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NEW ISC Accountancy

Class XII
(In Two Volumes)

Vol. I Partnership Accounts

AVICHAL PUBLISHING COMPANY

NEW ISC ACCOUNTANCY

FOR CLASS XII

(IN TWO VOLUMES)

[Strictly according to the latest syllabus prescribed by the Council for Indian School Certificate Examinations, New Delhi for the examination to be held in 2023.]

VOLUME I

Scan QR CODES for additional Illustrations and Questions

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PREFACE TO THE REVISED EDITION

It gives us immense pleasure to present the thoroughly revised edition of the book prepared in accordance with the new revised syllabus and examination pattern prescribed by the ISC for 2023 examination.

To ensure that the size of the book does not unduly increase as we need to add fresh Illustrations and Practical Questions in each chapter, we have provided additional Illustrations and Questions through QR Codes to help the students.

The book has several unique features which make it distinct from other available books on Accountancy.

Some of the special features of the book are :

1. A number of illustrations have been given in each chapter and these have been solved in such a simple manner that students can easily understand them.
2. Practical questions given at the end of each chapter are strictly in the serial order of the illustrations. Answers and hints to solve the questions have been given at the end of each question. We are very much confident that after doing the illustrations, students can solve the practical questions independently.
3. The book contains Short-answer type, Multiple Choice Questions and Practical Questions at the end of each chapter so that students may test their understanding of the chapter.
4. Questions from the last ten years ISC Examination Question Papers have been incorporated in the respective chapters.
5. Weightage to each topic has been given according to the marks allotted to it by ISC.
6. Accuracy is one of the main features of the book.

We express our sincere thanks to the teachers and students for their valuable suggestions and to M/s Avichal Publishing Company for the support and encouragement provided by them. Suggestions for improvement in the book will be thankfully received and acknowledged.

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SYLLABUS IN ACCOUNTS

Prescribed by the Council for I.S.C., New Delhi

*There will be **two** papers in the subject.*

Paper I – Theory : 3 hours .....*80 marks*

Paper II – Project Work .....*20 marks*

PAPER – I (THEORY) – 80 MARKS

There will be one paper of 3 hours duration of 80 marks divided into three Sections A, B and C.

*It will be **compulsory** for all candidates to attempt **Section A.***

***Section A (60 Marks) :** will consist of **two** parts, **Part I** and **Part II** and have a total of **eight** questions.*

***Part I (12 Marks) :** will consist of **Question 1 (compulsory).** This question will include short answer questions, testing knowledge, application and skills relating to elementary/fundamental aspects. Question I will be based on **Section A** of the syllabus.*

***Part II (48 marks) :** Candidates will be required to answer **four** questions out of **seven** from this part. Each question shall carry **12 marks.** Part II will also be based on **Section A** of the syllabus.*

Section B/C (20 Marks) :** Candidates will have a choice of attempting questions **either** from **Section B** or **Section C.** Candidates will be required to answer **two** questions out of **three** from the section of their choice. Each question shall carry **10 marks.

SECTION A

1. Partnership Accounts

A. Fundamentals of Partnership

(i) Definition, meaning and features of a Partnership.
Self explanatory

(ii) Provisions of the Indian Partnership Act, 1932, with respect to books of accounts.

(a) *Meaning and importance.*

(b) *Rules applicable in the absence of a partnership deed.*

(iii) Preparation of Profit and Loss Appropriation Account and Partners' Capital and Current Accounts.

(a) *Profit and Loss Appropriation Account.*

(b) *Partners' capital accounts : fixed and fluctuating.*

(c) *Partners' Current Accounts when fixed capital method is followed.*

Interest on capital, interest on drawings, interest on current accounts (debit and credit), salary, commission to partners and managers, transfer to reserves, division of profit among partners.

(d) *Guarantee of profits*

(e) *Past adjustments (Relating to interest on capital, interest on drawing, salary and Profit Sharing Ratio).*

NOTE :

- *Interest on loan given by the partner to the firm is to be taken as a charge against profits. This interest will be debited to the P & L account and credited to his loan account.*
- *Interest on loan taken by a partner from the firm should be credited to P & L account and debited to his capital/current account as the case may be.*
- *Rent due to a partner is a charge against profit and is to be credited to partners' current account in case of fixed capital system or to partners' capital account when capitals are fluctuating.*
- *Rectification of errors (past adjustments) through a single journal entry/adjusting and closing journal entries, preparation of partner's adjusted Capital/Current Accounts.*
- *Admission of manager as a partner is excluded from the topic of past adjustments/guarantee of profit.*

B. Goodwill

Concept of goodwill and mode of valuation.

(a) *Meaning, nature and features of Goodwill.*

(b) *Factors affecting the value of goodwill.*

(c) *Mode of Valuation.*

- *Average profit method : Meaning and practical application.*
  - *Simple average.*
  - *Weighted average method.*
- *Super profit method : Meaning and practical application.*
- *Capitalization method : Meaning and practical application.*
  - *Capitalization of average profit.*
  - *Capitalization of super profit.*

NOTE :

Capital Employed/Net assets are Total assets (excluding purchased goodwill non-trade investments and fictitious assets) less outside liabilities. Investments to be taken as non-trade investments unless specified as trade investments.

C. Reconstitution of Partnership

1. Admission

(*i*) Calculation of new profit sharing ratio, sacrificing ratio and gaining ratio.

Self Explanatory

(*ii*) Accounting treatment of goodwill on admission of a partner.

Based on Accounting Standard – 26 issued by the Institute of Chartered Accountants of India in the context of Intangible Assets.

(a) *Premium for goodwill paid privately.*

(b) *Premium for goodwill paid (in cash or kind) and retained in the business.*

(c) *Premium for goodwill paid and withdrawn by the old partners.*

(d) *When the incoming partner cannot bring premium for goodwill in cash, adjustments are to be done through his current account.*

(e) *Hidden goodwill.*

(f) *When goodwill appears in the old Balance Sheet.*

(*iii*) Preparation of Revaluation Account.

Preparation of a Revaluation Account where changes in the values of assets and liabilities are reflected in the new Balance Sheet after reconstitution of a partnership firm.

(iv) Accounting treatment of accumulated profits and losses.

General Reserve/Reserve fund, Workmen Compensation Reserve/ Fund, Investment Fluctuation Reserve/Fund, Contingency Reserve, Profit and Loss Account (Debit and Credit balance) and Advertisement Suspense Account/Deferred Revenue Expenditure.

(v) Adjustment of Capitals.

(a) *Adjustment of old partner's Capital Accounts on the basis of the new partner's capital.*

(b) *Calculation of new partner's capital on the basis of old partner's adjusted capital.*

(vi) Change in profit sharing ratio.

Change in Profit Sharing Ratio takes place at the time of admission of a partner in partnership firm.

Accounting treatment of accumulated profits and losses — through one journal entry : (Adjustment of the incoming partners' share to be done through his Current Account — Similar to the treatment of goodwill not brought in cash)

Gaining Partners Capital/Current A/c Dr.

To Sacrificing Partners Capital/Current A/c

(In case of profit)

Sacrificing Partners Capital/Current A/c Dr.

To Gaining Partners' Capital/Current A/c

(In case of losses)

General Reserve/Reserve Fund, Workmen Compensation Reserve/ Fund, Investment Fluctuation Reserve/Fund, Contingency Reserve, Profit and Loss Account (Debit and Credit Balance) and Advertisement Suspense Account/Deferred Revenue Expenditure.

NOTE :

- Preparation of Balance Sheet during admission of a partner to be done in Horizontal format.
- Memorandum Revaluation Account, Joint Life Policy, Individual Life Policy are excluded from the Syllabus.
- Admission of a partner during an accounting year is excluded from the Syllabus.

II. Retirement and death of a partner

(i) Calculation of new profit sharing ratio, gaining ratio and sacrificing ratio.
Self Explanatory.

(ii) Adjustment with regard to goodwill including hidden goodwill.
Self Explanatory.

(iii) Adjustment with regard to undistributed profits and losses.

Self Explanatory.

(iv) Adjustment with regard to share of profits of the retiring or deceased partner from the date of the last Balance Sheet to the date of retirement or death (on the basis of time or turnover).

Through P & L Suspense A/c (in Case of no Change in Profit Sharing Ratio of remaining partners)

Through Gaining Partners Capital/Current A/c (in case of change in Profit Sharing Ratio of remaining partners)

(v) Preparation of Revaluation Account on retirement or death of a partner.

Self Explanatory.

(vi) Adjustment of capitals.

(a) *Readjusting the adjusted capital of the continuing partners in the new profit sharing ratio.*

(b) *Adjusting the capitals of the continuing partners on the basis of the total capital of the new firm.*

(c) *When the continuing partners bring in cash to pay off the retiring partners.*

(vii) Calculation and payment of amount due to retiring partner.

Self Explanatory.

(viii) Preparation of retiring partner's loan accounts and deceased partner's executor's loan account (with interest on loan accrued and due and interest on loan accrued but not due).

Self Explanatory.

(ix) Change in Profit Sharing Ratio.

Change in PSR takes place at the time of retirement / death of a partner.

Accounting treatment of accumulated profits and losses through one journal entry :

Gaining Partner's Capital/Current A/c Dr.

To Sacrificing Partners Capital/Current A/c

(in case of profits)

Sacrificing Partner's Capital/Current A/c Dr.

To Gaining Partner's Capital/Current A/c

(in case of losses)

General Reserve/Reserve Fund, Workmen Compensation Reserve/Fund, Investment Fluctuation Reserve/Fund, Contingency Reserve, Profit and Loss Account (Debit and Credit Balance) and Advertisement Suspense Account/Deferred Revenue Expenditure.

NOTE :

— *Preparation of Balance Sheet during retirement/death of a partner to be done in Horizontal Format only.*

— *Memorandum Revaluation Account, Joint Life Policy, Individual life policy are excluded from the syllabus.*

III. Dissolution of a Partnership firm.

(*i*) Meaning of dissolution and settlement of accounts under Section 48 of the Indian Partnership Act, 1932.

Self Explanatory.

(*ii*) Preparation of Memorandum Balance Sheet, Realization Account, Partner's Loan Account, Partner's Capital Accounts and Cash/Bank Account.

Self Explanatory.

NOTE :

- *When an asset or a liability is taken to the realization account any corresponding/related fund or reserve is also transferred to realization account and not to capital account.*
- *When accounts are prepared on a fixed basis, partners' current account balances are to be transferred to capital account. No adjustments are required to be passed through current account.*
- *Bank overdraft is to be taken to Bank/Cash A/c and not to be transferred to realization account but bank loan must be transferred to realization account.*
- *If question is silent about the payment of a liability, then it has to be paid out in full.*
- *If the question is silent about the realization of an asset, its value is assumed to be nil.*
- *Loan taken from a partner will be passed through Cash or Bank Account even if the partner's capital account has a debit balance.*
- *Loan given to a partner will be transferred (debited) to his Capital Account.*
- *Admission cum retirement, amalgamation of firms and conversion/sale to a company together with piecemeal distribution and insolvency of a partner/partners not required.*

2. Joint Stock Company Accounts

A. Issue of Shares.

Problems on issue of shares.

(*a*) Issue of shares at par and at premium under Companies Act, 2013.

(*b*) Issue of shares for considerations other than cash :

- To promoters (can be considered either through Goodwill account or Incorporation costs account).

- To underwriters.
- To vendors.

(c) Calls in arrears, calls in advance and interest thereon.

(d) Over and under subscription (including pro-rata allotment).

(e) Preparation of Journal, Cash Book and Journal Proper; Ledger Accounts.

NOTE : In pro-rata allotment when shares are issued at a premium, excess money received on application will first be adjusted towards the share capital. Any excess thereon will be utilized towards the securities premium reserve.

When allotment or any call money is due, it is to be transferred to the calls in arrears account, on which interest if provided in the Articles of Association will be calculated.

(f) Forfeiture and reissue of shares at par, premium or discount. *Self Explanatory.*

(g) Disclosure of Share Capital in the Company's Balance Sheet.

NOTE : Issue of bonus and rights shares, private placement of shares, sweat equity shares, employees' stock option scheme, reservations for small individual participants and minimum tradable lots are not required.

B. Issue of Debentures

Problems on issue of debentures (at par, at premium and at discount).

Problems on issue of debentures to include :

(a) *Issue of debentures at par, at premium and at discount under Companies Act 2013.*

(b) *Issue of debentures as collateral security for a loan.*

(c) *Issue of debentures for considerations other than cash.*

- To promoters
- To underwriters
- To vendors

(d) *Accounting entries at the time of issue when debentures are redeemable at par and premium.*

(e) *Calls in arrears, Calls in advance and interest thereon.*

(f) *Interest on debentures (with TDS).*

(g) *Disclosure of Debentures in the Company's Balance Sheet.*

(h) *Methods of writing off discount/loss on issue of debentures — when debentures are redeemable in a lump sum at the end of a specified period; when debentures are redeemable in instalments.*

(i) *Disclosure of discount on issue of debentures in the company's Balance Sheet when debentures are redeemed in instalments.*

C. Redemption of Debentures

- *Creation of Debenture Redemption Reserve (DRR) (Wherever applicable).*
- *Redemption of debentures out of profits.*
- *Redemption of debentures out of capital.*
- *Redemption of debentures in a lump sum.*
- *Redemption of debentures in annual instalments by draw of lots.*
- *Redemption of debentures by purchase in the open market for immediate cancellation; as an investment and then later cancelled.*

Self Explanatory.

NOTE :

I. Calculation of ex-interest and cum-interest are not required.

II. In case of redemption of debentures in annual instalments by draw of lots :

(*i*) The entire DRI purchased for the redemption of the instalment of debentures is not sold at the end of the year but sold/further purchased to the extent to maintain 15% of the face value of the debentures to be redeemed in the next instalment. In case of redemption in equal instalments, DRI purchased for the first instalment remains invested till the last instalment.

(*ii*) Wherever applicable, DRR is transferred to General Reserve in proportion to the debentures redeemed.

III. Rules relating to creation of Debenture Redemption Reserve (DRR) :

(*i*) Listed companies including NBFCs registered with RBI and HFCs registered with National Housing Bank (NHB) both for public issue as well as private placements do not require the creation of a DRR of 25 per cent of the value of outstanding non-convertible debentures.

(*ii*) Unlisted NBFCs registered with RBI and HFCs registered with National Housing Bank (NHB) both for public issue as well as private placements do not require the creation of a DRR of 25 per cent of the value of outstanding non-convertible debentures.

(*iii*) For unlisted companies (other than NBFCs and HFCs), DRR is reduced from the present level of 25 per cent to 10 per cent of the outstanding debentures.

Rules regarding Debenture Redemption Investment (DRI)

- Unlisted NBFCs and HFCs need not deposit any amount of its debentures maturing during the year with scheduled banks or invest it in specified government securities.

- The following companies will continue to invest or deposit, on or before 30th April in each year, a sum which shall not be less than 15 per cent, of the amount of its debentures maturing during the year, ending on 31st March of the next year, in deposits with any scheduled bank, free from any charge or lien / in unencumbered securities of the Central Government or any State Government / in unencumbered securities mentioned in Section 20 of the Indian Trusts Act, 1882 / in unencumbered bonds issued by any other company notified under Section 20 of the Indian Trusts Act, 1882 :

    (*i*) Listed companies including NBFCs registered with RBI, HFCs National Housing Bank (NHB) and unlisted companies (other than NBFCs and HFCs).

    (*ii*) Unlisted companies (other than NBFCs and HFCs).

Basically, All India Financial Institutions regulated by RBI, Banking Companies for both public as well as privately placed debentures, other Financial Institutions within the meaning of Section 2(72) of the Companies Act, 2013 and unlisted NBFCs registered with RBI and HFCs registered with National Housing Bank (NHB) are exempted both from creating DRR and from making a DRI.

D. Final Accounts of Companies

Preparation of the Balance Sheet of a Company (along with notes to accounts) as per Schedule III Part I of Companies Act, 2013.

As per the amendment made in Accounting Standard 4, dividend proposed for a year is not a liability till it has been approved by the shareholders. Thus, proposed dividend is not shown as a short-term provision in the current Balance Sheet of a company but disclosed in Notes to Accounts under Contingent Liabilities.

All capital losses to be written off in the year in which they occur unless otherwise mentioned.

NOTE :

Schedule III Part II of Companies Act 2013 (Statement of Profit and Loss) is not required for the purpose of preparing Final Accounts of a Company.

However, for the preparation of Comparative and Common Size Income Statements (Section B – Unit 4 : Financial Statement Analysis), the extent and format of the Statement of Profit and Loss as per Schedule III Part II of the Companies Act 2013 to be studied, is as follows :

Profit and loss statement for the year ended ....

(₹ in ....)

	Particulars	Note No.	Figures for the current reporting period	Figures for the previous reporting period
I.	Revenue from operations		XXX	XXX
II.	Other Income		XXX	XXX
III.	Total Revenue (I + II)		XXX	XXX
IV.	Expenses :			
	Cost of materials consumed		XXX	XXX
	Purchases of Stock-in-Trade		XXX	XXX
	Changes in inventories of finished goods, work-in-progress and Stock-in-Trade		XXX	XXX
	Employee benefits expenses			
	Finance costs			
	Depreciation and amortization expenses			
	Other expenses			
	Total expenses		XXX	XXX
V.	Profit before Tax (III–IV)		XXX	XXX
VI.	Tax		XXX	XXX
VII.	Profit after Tax (V–VI)		XXX	XXX

SECTION B
MANAGEMENT ACCOUNTING

3. Financial Statement Analysis

Comparative Statements and Common Size Statements.

Meaning, significance and limitations of Comparative Statements and Common Size Statements.

Preparation of Comparative Balance Sheet and Statement of Profit and Loss (inter-firm and intra-firm) showing absolute change and percentage change.

Common size Balance Sheet to be prepared as a percentage of total assets and total liabilities.

Common size Statement of Profit and Loss to be prepared as a percentage of Revenue from Operations.

***NOTE** : Preparation of comparative statements and common size statements to be made from the Balance Sheets and Statement of P & L without notes to accounts.*

4. Cash Flow Statement (Only for Manufacturing Companies)

(*i*) Meaning, importance and preparation of a Cash Flow Statement.

NOTE : *Based on Accounting Standard – 3 (revised) issued by the Institute of Chartered Accountants of India.*

(*ii*) Calculation of net cash flows from operating activities based on Indirect Method only.

Preparation of a Cash Flow Statement from two consecutive years' Balance Sheet with or without adjustments.

Preparation of complete/partial cash flow statement from extracts of Balance Sheets and Statements of P & L with or without adjustments.

NOTE : *Any adjustment or an item in the Balance Sheet relating to issue of bonus shares; Extraordinary items and refund of tax are not required.*

(*iii*) Preparation of Cash Flow Statement on basis of operating, investing and financing activities :

The following items are to be taken when calculating net cash flows from financing activities.

- *Issue of shares at par and premium, issue of debentures at par, premium and discount.*
- *Redemption of preference shares, and debentures at par.*
- *Interest paid on Long-Term and Short-Term Borrowings.*
- *Dividend — interim and final — paid on shares.*
- *Long-term borrowings and Short-term borrowings — bank overdraft, cash credit and short-term loan, whether taken or repaid.*
- *Share issue expenses/underwriting commission paid.*

The following items are to be taken when calculating net cash flows from investing activities :

- *Cash purchase of fixed assets.*
- *Cash sale of fixed assets.*
- *Purchase of shares or debentures or long term investments of other companies.*
- *Interest and dividend received on shares or debentures or long term investments of other companies.*
- *Sale of shares or debentures or long term investments of other companies.*

The following items are to be taken for cash and cash equivalents :

- *Cash*
- *Bank*

- *Short term investments*
- *Marketable securities*

NOTE :

(i) *Adjustments relating to provision for taxation, proposed dividend, interim dividend, amortization of intangible assets, profit or loss on sale of fixed assets including provision for accumulated depreciation on them, profit or loss on sale of investment are also included.*

(ii) *Treatment of proposed dividend :*

(a) *Dividend proposed for the previous year will be an outflow for cash, unless otherwise stated, on the assumption that the proposed amount has been approved by the shareholders in the AGM.*

(b) *No effect is given to Proposed Dividend for the current year as it is not provided for and is a contingent liability.*

(c) *Any unpaid dividend is transferred to Dividend Payable Account / Unpaid Dividend Account which is shown in the Balance Sheet of the current year as Other Current Liabilities under Current Liabilities.*

(iii) *Treatment of provision for doubtful debts — Provision for doubtful debts can be treated as a charge against profits or as part of the working capital changes. In case of good debtors, the provision will be treated as an appropriation of profit.*

(iv) *To calculate cash flow from operating activities the Adjusted Profit and Loss Account is not acceptable as per AS-3.*

(v) *Calculation of Net Profit before Tax has to be shown as a Working Note.*

(vi) *Excluded : Any transaction pertaining to Capital Reserve.*

5. Ratio Analysis

(a) Liquidity Ratios :

1. Current Ratio : $\dfrac{\text{Current Assets}}{\text{Current Liabilities}}$

Current Assets = Current Investments + Inventories (excluding Loose Tools and Spare Parts) + Trade Receivables + Cash and Bank Balance + Short-term Loans and Advances + Other Current Assets

Current Liabilities = Short term borrowings + Trade Payables + Other Current Liabilities + Short term Provisions

2. ***Quick Ratio / Liquid Ratio :*** $\dfrac{\text{Quick Assets}}{\text{Current Liabilities}}$

OR

$$\frac{\text{All Current Assets} - \text{Inventories (excluding Loose Tools and Spare Parts)} - \text{Prepaid Expenses}}{\text{Current Liabilities}}$$

OR

$$\frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

(b) Solvency Ratios :

1. ***Debt to Equity Ratio :*** $\dfrac{\text{Debt / Long Term Debt}}{\text{Equity / Shareholder's Funds}}$

Debt = Long Term Borrowings + Long Term Provisions

Equity / Shareholder's Funds = Share Capital + Reserves and Surplus

Or

= Non Current Assets + (Current Assets – Current Liabilities) – Non Current Liabilities

Or

= Non Current Assets + Working Capital – Non Current Liabilities

Or

= (Tangible Assets + Intangible Assets + Non Current Investments + Long Term Loans and Advances) + Working Capital – (Long Term Borrowings + Long Term Provisions)

2. ***Proprietary Ratio :*** $\dfrac{\text{Shareholder's Funds / Equity}}{\text{Total Assets}}$

Total Assets = Non Current Assets + Current Assets

= Tangible Assets + Intangible Assets + Non Current Investments + Long Term Loans and Advances + Current Investments + Inventories (including Loose Tools and Spare Parts) + Trade Receivables + Cash and Bank Balance + Short-term Loans and Advances + Other Current Assets

3. ***Debt to Total Assets Ratio :*** $\dfrac{\text{Debt}}{\text{Total Assets}}$

4. ***Interest Coverage Ratio :*** $\dfrac{\text{Net Profit before Interest and Taxes}}{\text{Fixed Interest Charges}}$

Fixed Interest charges includes interest on only long term borrowings.

(c) Activity Ratios :

1. ***Trade Receivables Turnover Ratio :***

$$= \frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivable}}$$

Credit revenue from Operations = Revenue from Operations – Cash Revenue from Operations

Average Trade Receivables =

$$\frac{\text{Opening Trade Receivable} + \text{Closing Trade Receivable}}{2}$$

2. ***Trade Payables Turnover Ratio :*** = $\dfrac{\text{Net Credit Purchases}}{\text{Average Trade Payables}}$

Average Trade Payables =

$$\frac{\text{Opening Trade Payable} + \text{Closing Trade Payable}}{2}$$

3. ***Working Capital Turnover Ratio :*** $\dfrac{\text{Revenue from Operations}}{\text{Working Capital}}$

4. ***Inventory Turnover Ratio*** = $\dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

Cost of Revenue from Operations = Revenue from Operations – Gross Profit

Or

Cost of Meterial Consumed (including direct expenses) + Change in inventories of WIP and Finished Goods

Or

Opening Inventory + Net Purchases + Direct Expenses – Closing Inventory

$$\text{Average Inventory} = \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$$

(d) Profitability Ratios :

1. Gross Profit Ratio : $\dfrac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$

Gross Profit = Revenue from Operations – Cost of Revenue from Operations / Cost of Goods sold

Cost of Revenue from Operations = Cost of Material Consumed (including direct expenses) + Change in inventories of WIP and Finished Goods

Or

Opening Inventory + Net Purchases + Direct Expenses – Closing Inventory

2. Net Profit Ratio : $\dfrac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$

Net Profit = Gross Profit + Other Income – Indirect Expenses – Provision for Tax

3. Operating Ratio :

$$= \frac{\text{Cost of Revenue from Operations} + \text{Operating Expenses}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{\text{Cost of Revenue from Operations} + \text{Operating Expenses} - \text{Operating Income}}{\text{Revenue from Operations}} \times 100$$

Operating Expenses = Employee Benefit Expenses + Depreciation of Tangible Assets + Selling and Distribution Expenses + Office and Administrative Expenses

Operating Income = Commission received, Cash discount received.

4. Operating Profit Ratio : $= \dfrac{\text{Net Operating Profit}}{\text{Revenue from Operations}} \times 100$

Net Operating Profit = Net Profit after Tax + Provision for Tax + Non-Operating Expenses – Non Operating Incomes

Or

Gross Profit – Operating Expenses + Operating Incomes

Non Operating Expenses = Finance Cost (Interest on Long-term Borrowings) + Loss on sale of Non Current Assets + Amortization of Intangible Assets + Writing off Capital Losses.

Non Operating Incomes = Interest and Dividend Received on Investment + Profit on sale of Non Current Assets

5. *Earning per share :*

$$\frac{\text{Net Profit after Tax and Preference Dividend}}{\text{No. of Equity Shares}}$$

6. *Price Earning Ratio :*

$$\frac{\text{Market Value of an Equity Share}}{\text{Earning Per Share}}$$

7. *Return on Investment :*

$$\frac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$$

NOTE :

1. *Current Ratio includes Net Debtors (Gross Debtors – Provision for doubtful debts) while Trade Receivables Turnover Ratio includes Gross Debtors.*
2. *Other Current Assets is restricted to Prepaid Expenses and Accrued Income.*
3. Capital Employed = Shareholder's Funds + Non Current Liabilities – Non Trade Investments.

   OR Non-Current Assets (excluding non trade investments) + Working Capital

   OR Fixed Assets + Trade Investments + Working Capital
4. *Investments to be taken as non-trade investments unless specified as trade investments.*
5. In Return on Investment Ratio — Net Profit before Interest and Tax will not include interest on non-trade investments.

6. Revenue from Operations (for a manufacturing Company)

- Net Sales
- Sale of Scrap

For a manufacturing company

Other Income (for a manufacturing company)

- Rent received (non-operating)
- Commission received (operating)
- Interest and Dividend Received (non-operating)
- Profit on Sale of Fixed Assets (non-operating)
- Cash discount received (operating)

7. Problems on effect of transactions on ratios to be restricted to Current Ratio, Quick Ratio and Debt Equity Ratio.
8. Net Profit Ratio is to be calculated on 'Net Profit after Tax'.

Paper II – Project Work – 20 Marks

Candidates will be expected to have completed **two** projects from any topic covered in Theory.

The project work will be assessed by the teacher and a Visiting Examiner appointed locally and approved by the Council.

Mark allocation for **each** Project (10 marks) :

Overall format	1 mark
Content	4 marks
Findings	2 marks
Viva-voce based on the Project only	3 marks

A. list of suggested Projects is given below :

1. Preparation of Journal/Sub-division of Journal, Ledger, Trial balance and Financial Statements of a partnership form of business on the basis of a case study.
   - Develop a case study showing how two or more friends decide to come together and start a business with a certain amount of capital.
   - Prepare their Partnership Deed including interest on Capital, partner's salary, commission, interest on drawings, interest on partner's loan and rent paid to a partner.
   - Write in detail, their transactions during the year : purchases – cash and credit, sales – cash and credit, expenses, purchase of fixed assets and depreciation charged on them, any outstanding expenses, prepaid expenses, accrued income, drawing bills of exchange, accepting bills payable etc.
   - From this case study developed (which should have at least 15 transactions), pass the journal entries, post them into the ledger, prepare a Trial Balance and the Trading and Profit and Loss Account, Profit and Loss Appropriation Account and Balance Sheet.
   - The various expenses, for comparison purpose, could be depicted in the form of bar diagrams, pie charts.
   - Calculate relevant accounting ratios like liquidity, solvency, activity and profitability – giving their formulae and computation (all this could be part of the viva-voce).
   - The ratios could also be shown graphically and/or pictorially (bar diagrams, pie charts) and if possible, could be compared with the ratios of the industry.

2. Preparation of a Cash Flow Statement with the help of audited/ unaudited/imaginary Balance Sheets of a company for two consecutive accounting years or two consecutive quarters of an accounting year could be taken along with at least five additional information (depreciation, purchase/sale of fixed assets, Dividend paid/proposed, Tax paid/proposed, amortization of intangible assets, profit or loss on sale of fixed assets including provision for depreciation on them and profit or loss on sale of investment).

   - The results of the operating, investing and financing activities could be shown graphically and/or pictorially (bar diagrams and pie charts).

3. Preparation of Common Size and Comparative Income Statement of Profit and Loss and Balance Sheet of a company by taking into account its audited/unaudited/imaginary financial results of two consecutive quarters of an accounting year or of two consecutive accounting years.

   - The comparison has to be made in the form of Common Size and Comparative Income Statement and Balance Sheet.
   - The comparison could also be shown graphically and/or pictorially (bar diagrams, pie charts).

4. Taking the audited/unaudited/imaginary financial results of any leading company, its liquidity, solvency, activity and profitability ratios of two consecutive years or of two consecutive quarters of an accounting year should be calculated and the comparison of the ratios of both the years or quarters should be shown graphically and/or pictorially (bar diagrams, pie charts).

NOTE : No question paper for Practical Work will be set by the Council.

CONTENTS

VOLUME I

VOLUME II

(In Separate Binding)

QR Code for Additional Illustrations and Questions related to Chapter 6 to 14 are provided in Vol. II

1

Accounting for Partnership Firms — Fundamentals

LEARNING OBJECTIVES

After studying this Chapter you should be able to understand :

- **Nature of Partnership Firm**
- **Definition and Main Features of Partnership**
- **Partnership Deed — Meaning, Importance**
- **Methods of Preparing Capital Accounts of Partners under Fixed and Fluctuating Capital Methods**
- **Division of Profit among Partners**
- **Profit and Loss Appropriation Account**
- **Past Adjustments**
- **Guarantee of Minimum Profit to a Partner**

Introduction : There are certain limitations of a sole trader. In a sole trading concern only one man invests capital, undertakes the risk involved in the business and controls the whole affairs of the business. But one man's capital, skill, controlling and risk taking capacity are generally limited. Therefore, some persons may combine and enter into an agreement to form a partnership.

Partnership is a relation of mutual trust and faith. In order to maintain this trust, it is necessary that the partnership accounts be maintained in an honest, accurate and equitable manner. Partnership accounts should present a **true and fair** picture of the partnership business. For this purpose it is necessary to study the definition of partnership as given in the Partnership Act and the relevant provisions of the Partnership Act which affect the partnership accounts.

Nature of Partnership Firm :

As per Accounting viewpoint, partnership firm is treated as a separate business entity distinct from its partners. However, as per legal viewpoint, a partnership firm is not a separate legal entity. In other words, it has no existence separate from its partners. It means that in case of bankruptcy of the partnership firm, private estates of the partners would be liable to meet the firm's debts.

Definition of Partnership : Section 4 of the Indian Partnership Act, 1932, defines partnership as follows :

"Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all."

Main Features or Characteristics of Partnership

1. **Two or more persons :—** There must be atleast two persons to form a partnership and such persons must be competent to contract. As per the Indian Contract Act, 1872 every person except the following are competent to contract :

(*a*) Minor

(*b*) Persons of unsound mind, and

(*c*) Persons disqualified by any law

Maximum Number of Partners :

Partnership Act does not specify the maximum number of partners, but the Central Government has prescribed maximum number of partners in a firm to be 50 vide rule 10 of the Companies (Miscellaneous) Rules, 2014.

Minor as a partner :

A minor cannot be admitted as a partner in the firm. However, he is allowed to participate in the profits of the firm.

2. **Agreement :—** Partnership is the result of an agreement. It must come into existence by an agreement and not by the operation of law. On the contrary, a Hindu undivided family comes into existence by the operation of law and not by an agreement. Such an agreement can be either oral or in writing. The agreement forms the basis of mutual rights and duties of partners.

3. **Existence of Business and Profit Motive :—** Partnership can be formed for the purpose of carrying on some business with the intention of earning profits and such business must be legal. A joint ownership of some property by itself cannot be called a partnership.

4. **Sharing of Profits :—** The agreement between the partners must be aimed at sharing the profits of the business. If some persons join hands to run some charitable activity, it will not be called partnership. Further, if a partner is deprived of his right to share the profits of the business, he cannot be called a partner. But it is not necessary that all partners should share the losses also. It may be agreed between the partners that one or more of them shall not be liable for losses.

5. **Relationship of Principal and Agent :—** Each partner is an agent as well as a principal of the firm. An agent, because he can bind the other partners by his acts and a principal, because he himself can be bound by the acts of the other partners.

6. **Business may be carried on by all or any of them acting for all :—** It means that each partner can participate in the conduct of business and each partner is bound by the acts of other partners in respect to the business of the firm.

7. **No Separate Existence :—** A partnership firm has no separate existence from its members. It means that all agreements entered with the firm will be enforceable against each partner separately and jointly. However, partnership firm is a separate business entity from accounting point of view.

Partnership cannot come into existence in the absence of any one of the above mentioned essential features.

Rights of a Partner :

1. Every partner has the right to share profits or losses with other partners in the agreed ratio.
2. Every partner has the right to take part in the conduct of the business.
3. Every partner has the right to be consulted in the matters related to partnership business.
4. Every partner has the right to inspect and have a copy of the books of accounts.
5. Every partner has a right to disallow the admission of a new partner.
6. Every partner is the joint owner of the partnership property.
7. If a partner has given loan to the firm, he has a right to receive interest at agreed rate. If the rate of interest is not agreed, it is paid @6% p.a.
8. If a partner incurs expenses or makes payment on behalf of the firm, he has a right to be indemnified by the firm.
9. Every partner has a right to retire from the firm after giving a proper notice.

Partnership Deed

Since partnership is the outcome of an agreement, it is essential that there must be some terms and conditions agreed upon by all the partners. Such terms and conditions may be either oral or written. The law does not make it compulsory to have a written agreement. However, in order to avoid all misunderstandings and disputes, it is always the best course to have a written agreement duly signed and registered under the Act. Such a written document which contains the terms of agreement is called **'Partnership Deed'**. It is also called **'Articles of Partnership'**. The partnership deed should contain the following points :

(1) **The Name and Address of the Firm.**

(2) **Names and Addresses of the Partners.**

(3) **The Type and Nature of the Business the Firm Proposes to do.**

(4) **Amount of Capital to be Contributed by each Partner and** whether the capital accounts will be fixed or fluctuating.

(5) **Interest on Capitals :—** Whether interest is to be allowed on capitals. If so, the rate of interest.

(6) **Drawings :—** How much amount the partners are entitled to withdraw for personal use.

(7) **Interest on Drawings :—** Whether interest will be charged on partner's drawings. If so, the rate of interest.

(8) **Profit Sharing Ratio :—** The ratio in which profits or losses are to be divided among the partners.

(9) **Salary :—** Whether any partner will be paid salary for the work done by him. If so, how much?

(10) **Goodwill :—** Method of valuation of goodwill in case of admission or retirement of a partner.

(11) **Accounting Period of the Firm :—** The period after which the final accounts of the firm are to be prepared. Whether yearly or half-yearly and the date on which accounts are to be closed every year.

(12) **Method of Recording of Firm's Accounts** and the safe custody of the books of accounts and other documents of the firm.

(13) **Auditing :—** Whether the firm's books will be audited or not? If so, the mode of auditor's appointment.

(14) **Date of Commencement of partnership.**

(15) **Duration of Partnership :—** The period for which the partnership has been established and the mode of dissolution of partnership.

(16) **Use of the Decision of Garner Vs Murray :—** Whether decision in the case of Garner *Vs* Murray is to apply in the case of insolvency of a partner.

(17) **Bank Accounts :—** Whether the account in the bank will be opened in firm's name or in some partner's name? Who will have the right to sign the cheques?

(18) **Rules to be followed in case of Admission of a Partner.**

(19) **Rules to be followed while Settling the Accounts on Retirement :—** The manner in which the amount due on the retirement or death of a partner will be calculated and the manner in which it will be paid.

(20) **Settlement of Disputes :—** In case of dispute among the partners, how the dispute will be solved. Whether arbitrator will be appointed?

Importance of Partnership Deed :

Though, the law does not make it mandatory (compulsory) for every firm to have a partnership deed, it is desirable to have it due to the following reasons :

(*i*) It regulates the rights, duties and liabilities of each partner.

(*ii*) It helps to avoid any misunderstanding amongst the partners because all the terms and conditions of partnership have been laid down before hand in the deed.

(*iii*) Any dispute amongst the partners may be settled easily as the partnership deed may be readily referred to.

Hence, it is always the best course to have a written partnership deed duly signed by all the partners and registered under the Act.

Rules Applicable in the Absence of Partnership Deed

In the absence of a Partnership Deed or Verbal agreement, or if the Partnership Deed is silent on a certain point, the following provisions of Partnership Act, 1932 will be applicable :—

(1) **Profit-Sharing Ratio :—** Profits and Losses are to be shared equally irrespective of their capital contribution.

(2) **Interest on Capital :—** No interest on Capitals shall be allowed to the partners. If there is a provision for the interest on capitals in the partnership deed, it will be allowed only when there is a profit.

(3) **Interest on Drawings :**— No interest is to be charged on drawings.

(4) **Salary to a Partner :**— No partner is entitled to any salary or commission for taking part in running the firm's business.

(5) **Interest on Loan :**— Interest at the rate of 6% per annum is to be allowed on a partner's loan to the firm. Such interest shall be paid even if there are losses to the firm.

(6) **Admission of a New Partner :**— Without the consent of all existing partners no new partner can be admitted to the firm.

(7) Each partner can participate in the conduct of business.

(8) Each partner can inspect the books of firm and can take a copy of the same.

It should be remembered that partners may change any of the above provisions by coming to a common agreement.

Recording of Partnership Transactions

Transactions of the partnership firm are recorded according to the principles of double-entry system, and as in the case of a sole proprietorship concern a partnership firm will also prepare Trading Account, Profit & Loss Account and Balance Sheet at the end of every year. The only difference between accounting of a sole trader and partnership firm is that the profits of the partnership firm are divided among the partners. Usually, for this purpose, the profits as per Profit and Loss Account is transferred to a newly-opened account, namely 'Profit and Loss Appropriation Account' and entries for interest on capital, interest on drawing, salary to partners and division of profits among the partners will be passed only in that account. A specimen of Profit and Loss Appropriation Account showing the distribution of profits is given below :

PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended ....* Cr.

Particulars	₹	*Particulars*	₹
To Salaries of Partners		By Profit & Loss A/c	
To Commission to Partners		(Net Profit transferred from	
To Interest on Partner's Capitals :		P & L A/c)	
A		By Interest on Drawings :	
B		*A*	
To Reserve A/c		*B*	
To Profit transferred to :			
A's Capital A/c			
(or *A*'s Current A/c)			
B's Capital A/c			
(or *B*'s Current A/c)			

The journal entries that are passed for various items shown in the above Profit and Loss Appropriation Account are as follows :

1. Entry for transfer of Net Profit to Profit & Loss Appropriation Account :

Profit and Loss A/c ... Dr.
To Profit and Loss Appropriation A/c
(Net Profit transferred)

2. Entry for Interest on Capital :—

(*i*) On allowing Interest on Capital :
Interest on Capital A/c ... Dr.
To Partner's Capital A/c
(Interest on Capital at ....% p.a.)

(*ii*) On closure of Interest on Capital A/c :
Interest on capital is closed by transferring it to the debit side of Profit & Loss Appropriation A/c, as this is expenses for the firm. The entry will be :

Profit & Loss Appropriation A/c ... Dr.
To Interest on Capital A/c

3. Entry for Interest on Drawings :—

(*i*) On charging Interest on Drawings :
Partner's Capital A/c ... Dr.
To Interest on Drawings A/c

(*ii*) On closure of Interest on Drawings A/c :
Interest on Drawings is closed by transferring it to the credit side of Profit & Loss Appropriation A/c, as this is income for the firm. The entry will be :

Interest on Drawings A/c ... Dr.
To Profit & Loss Appropriation A/c

4. Entry for Salary or Commission Payable to a Partner :—

(*i*) On allowing salary or commission to a partner :
Partner's Salary/Commission A/c ... Dr.
To Partner's Capital A/c

(*ii*) On closure of salary or commission to a partner account :
Salary or Commission payable to a partner is closed by transferring it to the debit side of Profit and Loss Appropriation Account, as these are expenses for the firm. The entry will be :

Profit & Loss Appropriation A/c ... Dr.
To Partner's Salary/Commission A/c

5. Entry for transferring a part of profit to Reserve :

Profit & Loss Appropriation A/c ... Dr.
To Reserve A/c

6. Entry for transfer of Credit balance of Profit & Loss Appropriation A/c (being profit) :—

I. Profit & Loss Appropriation A/c ... Dr.
To Partner's Capital or Current A/cs

Features of Profit and Loss Appropriation Account :

1. It is prepared just after the Profit and Loss Account. Hence, it is an extension of Profit and Loss Account.
2. It is prepared only by partnership firms.
3. It is a Nominal Account.
4. It shows how the net profit for the accounting period is appropriated (distributed) among the partners.
5. Entries in this account are made giving effect to the Partnership Deed and/or the Indian Partnership Act, 1932.

Distinction between Profit & Loss Account and Profit & Loss Appropriation Account

	Basis of Distinction	*Profit & Loss Account*	*Profit & Loss Appropriation Account*
1.	**Stage of Preparation**	It is prepared after Trading Account and hence starts with the gross profit disclosed by Trading Account.	It is prepared after Profit and Loss Account and hence starts with the net profit disclosed by Profit & Loss Account.
2.	**Objective**	It is prepared to ascertain net profit or net loss.	It is prepared to show appropriation *i.e.* distribution of net profit of the year among the partners.
3.	**Opening/Closing Balance**	This account has neither opening balance nor closing balance.	This account may have opening as well as closing balances.
4.	**Charge or Appropriation**	Expenses debited to this account are charge against profits.	Expenses debited to this account are appropriation of profits.
5.	**Partnership Agreement**	This account is not prepared on the basis of partnership agreement, except for interest on loan from partners.	This account is prepared on the basis of partnership agreement.
6.	**Matching Principle**	Matching principle (i.e. matching of revenue against expenses) is followed while preparing this account.	Matching principle is not followed while preparing this account.

Attention

Any amount payable to a partner, such as salary, commission, interest on Capital etc. (except interest on Partner's Loan and rent payable to a partner) is treated as appropriation of profit and not a charge against profit. Hence, these items are debited to Profit & Loss Appropriation A/c instead of Profit & Loss A/c.

Distinction between Charge Against Profit and Appropriation out of Profit

	Basis of Distinction	*Charge Against Profit*	*Appropriation Out of Profit*
1.	**Nature**	It indicates expenses to be deducted from profits while calculating net profit or loss.	It indicates distribution of net profit to various heads.
2.	**Recording**	It is debited to Profit and Loss Account.	It is debited to Profit and Loss Appropriation Account.
3.	**Necessary or not**	It is necessary to make charges against profits even if there is loss.	Appropriations are made only when there is profit.
4.	**Example**	Interest on partner's loan and rent paid to a partner.	Interest on capital, partner's salary etc.

ILLUSTRATION 1.

Arti and Bharti are partners in a firm sharing profits in the ratio of 3 : 2. The following trial balance was extracted from their books as at 31st March, 2022 :

TRIAL BALANCE
as at 31st March, 2022

Dr. Balances	₹	*Cr. Balances*	₹
Opening Stock	36,000	Sales	9,40,000
Purchases	6,20,000	Returns Outwards	4,000
Returns Inwards	12,000	Sundry Creditors	43,000
Sundry Debtors	1,25,000	Interest	1,000
Computer	50,000	Arti's Capital	3,00,000
Rent (for 11 months)	22,000	Bharti's Capital	1,50,000
Salary to Staff	1,20,000		
Land & Building	3,52,000		
Wages	16,000		
General Charges	30,000		
Cash at Bank	25,000		
Arti's Drawings	20,000		
Bharti's Drawings	10,000		
	14,38,000		14,38,000

You are required to prepare the Trading, Profit and Loss Account and **Profit and Loss Appropriation Account** for the year ended 31st March, 2022 and a Balance Sheet as on that date, taking into account the following adjustments :

(*i*) Stock on 31st March, 2022 was valued at ₹60,000.

(*ii*) Rent for the month of March 2022 has not been paid.

(*iii*) Depreciate Computer by 20%.

(*iv*) Bharti is to be allowed a salary of ₹5,000 per month and partners are entitled to interest on Capital @ 6% p.a.

SOLUTION :

TRADING AND PROFIT & LOSS ACCOUNT OF THE FIRM

Dr. *for the year ended 31st March, 2022* Cr.

Particulars		₹	*Particulars*		₹
To Opening Stock		36,000	By Sales	9,40,000	
To Purchases	6,20,000		*Less* : Returns Inwards	12,000	9,28,000
Less : Returns Outwards	4,000	6,16,000	By Closing Stock		60,000
To Wages		16,000			
To Gross Profit c/d		3,20,000			
		9,88,000			9,88,000
To Rent	22,000		By Gross Profit b/d		3,20,000
Add : Outstanding			By Interest		1,000
(22,000 ÷ 11)	2,000	24,000			
To Salary to Staff		1,20,000			
To General Charges		30,000			
To Depreciation on Computer		10,000			
To Net Profit transferred to Profit & Loss Appropriation A/c		1,37,000			
		3,21,000			3,21,000

PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2022* Cr.

Particulars		₹	*Particulars*	₹
To Bharti's Salary		60,000	By Profit & Loss A/c	
To Interest on Capital :			(Net Profit)	1,37,000
Arti	18,000			
Bharti	9,000	27,000		
To Profit transferred to				
Arti's Capital A/c	30,000			
Bharti's Capital A/c	20,000	50,000		
		1,37,000		1,37,000

BALANCE SHEET OF THE FIRM

as at 31st March, 2022

Liabilities		₹	*Assets*		₹
Sundry Creditors		43,000	Cash at Bank		25,000
Outstanding Rent		2,000	Sundry Debtors		1,25,000
Arti's Capital	3,00,000		Closing Stock		60,000
Less : Drawings	20,000		Computers	50,000	
	2,80,000		*Less* : Depreciation	10,000	40,000
Add : Interest on Capital	18,000		Land & Building		3,52,000
Net Profit	30,000	3,28,000			

Bharti's Capital	1,50,000			
Less : Drawings	10,000			
	1,40,000			
Add : Salary	60,000			
Interest on Capital	9,000			
Net Profit	20,000	2,29,000		
		6,02,000		6,02,000

Interest on Capital :

As already stated, interest on partner's capitals is to be allowed only when it is expressly agreed to among the partners. If interest on capital is to be allowed as per agreement, it should be calculated with respect to the time, rate of interest and the amount of capital.

ILLUSTRATION 2.

Arun and Barun are partners in a firm sharing profits and losses equally. Their capitals on 1st April, 2015 were ₹4,80,000 and ₹5,40,000. On 1st October, 2015, they decided that the total capital of the firm should be ₹10,00,000 to be contributed equally by both of them. According to the partnership deed, interest on capital is allowed to the partners @6% p.a.

You are required to compute interest on capital for the year ending 31st March, 2016. *(ISC Sample Paper 2017)*

SOLUTION :

Calculation of Interest on Capitals : ₹

Arun : From 1st April, 2015 to 30th September, 2015

$$= ₹4,80,000 \times \frac{6}{100} \times \frac{6}{12} = 14,400$$

From 1st Oct., 2015 to 31st March, 2016

$$= ₹5,00,000 \times \frac{6}{100} \times \frac{6}{12} = 15,000$$

29,400

Barun : From 1st April, 2015 to 30th September, 2015

$$= ₹5,40,000 \times \frac{6}{100} \times \frac{6}{12} = 16,200$$

From 1st Oct., 2015 to 31st March, 2016

$$= ₹5,00,000 \times \frac{6}{100} \times \frac{6}{12} = 15,000$$

31,200

ILLUSTRATION 3.

A and *B* are partners in a firm. Their capital accounts showed the balance on April 1, 2019 as ₹4,00,000 and ₹3,00,000 respectively. On August 1, 2019 they introduced further capitals of ₹50,000 and ₹40,000 respectively. *B* withdrew ₹15,000 from his

capital on March 1, 2020. Interest is allowed @ 6% p.a. on the capitals. Compute interest on capitals for the year ending March 31, 2020.

SOLUTION :

Calculation of Interest on Capitals : ₹

A : On ₹4,00,000 for 4 months
(*i.e.*, from April 1, 2019 to 31st July, 2019)

$4,00,000 \times \frac{6}{100} \times \frac{4}{12}$ = 8,000

On ₹4,50,000 for 8 months
(*i.e.*, from August 1, 2019 to March 31st, 2020)

$4,50,000 \times \frac{6}{100} \times \frac{8}{12}$ = 18,000

26,000

B : On ₹3,00,000 for 4 months
(*i.e.*, from April 1, 2019 to 31st July, 2019)

$3,00,000 \times \frac{6}{100} \times \frac{4}{12}$ = 6,000

On ₹3,40,000 for 7 months
(*i.e.*, from August 1, 2019 to February 29th, 2020)

$3,40,000 \times \frac{6}{100} \times \frac{7}{12}$ = 11,900

On ₹3,25,000 for 1 month
(*i.e.*, from March 1, 2020 to March 31st, 2020)

$3,25,000 \times \frac{6}{100} \times \frac{1}{12}$ = 1,625

19,525

Capital Accounts of Partners

In case of partnership there is a separate Capital Account for each partner. The capital contributed by each partner will be credited to his capital account. The capital accounts of partners may be maintained in any one of the following two methods :

(1) Fixed Capital Accounts

(2) Fluctuating Capital Accounts

(1) **Fixed Capital Accounts :—** Under this system the original capitals invested by the partners remain constant, unless additional capital is introduced or drawings are made against capital by an agreement. In other words, capitals of the partners are not allowed to change during the life-time of business except in extraordinary circumstances. When fixed capital method is adopted, all entries relating to drawings against profits, interest allowed on capitals, interest charged on drawings, salary to partner, share of profit or loss etc., are made in a newly-opened account for each partner. This account is called Current Account or Drawings Account.

Thus, the following two accounts will be prepared separately when the capitals are fixed :

PROFORMA OF
CAPITAL ACCOUNTS (When the Capitals are fixed)

Dr. Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Cash/Bank A/c (Drawings against Capital or Permanent Withdrawal of Capital)				By Balance b/d (Opening Balance)			
To Balance c/d (Closing Balance)				By Cash/Bank A/c (additional Capital)			

CURRENT ACCOUNTS

Dr. Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Balance b/d (In case of debit opening balance)				By Balance b/d (In case of Credit opening balance)			
To Drawings (Drawings against profits)				By Interest on Capital			
To Interest on Drawings				By Partner's Salary			
To P & L A/c (Share of loss, in case of loss)				By Partner's Commission			
To Balance c/d*				By P & L Appropriation A/c (share of profit, in case of profit)			

* The balances may be on the opposite side also.

(2) **Fluctuating Capital Accounts** :— When the capitals need not be fixed, the balances of capital accounts go on changing from time to time. The reason is that no separate Current Accounts are maintained, but all the entries relating to drawings, interest on capitals, interest on drawings, salary to partner, share of profit or loss etc., are recorded in the capital accounts itself. **In the absence of information, the Capital Accounts should be prepared by this method.**

PROFORMA OF
CAPITAL ACCOUNTS (When the Capitals are fluctuating)

Dr. Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Cash/Bank (Drawings against Capital)				By Balance b/d (Opening Balance)			
				By Cash/Bank A/c			

To Drawings (Drawings against Profits) To Interest on Drawings To P & L A/c (Share of loss, in case of loss) To Balance c/d (Closing Balance)				(additional Capital) By Interest on Capital By Partner's Salary By Partner's Commission By P & L Appropriation A/c (share of profit, in case of profit)			

Current Accounts are not prepared when the Capitals are fluctuating.

Distinction Between Fixed Capital Accounts and Fluctuating Capital Accounts :

Basis of Distinction		Fixed Capital Accounts	Fluctuating Capital Accounts
1.	**Change in Capital**	When the Capitals are fixed, the balances in capital accounts usually remain unchanged during the life-time of business, except when Capital is introduced or withdrawn permanently.	When the Capitals are fluctuating, the balances in Capital Accounts go on changing from time-to-time.
2.	**Number of Accounts**	When the Capitals are fixed, each partner has two accounts, namely, Capital Account and a Current Account.	When the Capitals are fluctuating, each partner has only one account, namely, Capital Account.
3.	**Recording of Transactions**	When the Capitals are fixed, transactions relating to drawings, interest on Capital, interest on drawings, salary, share of profit or loss etc., are not made in Capital Accounts but are entered in separate Current Accounts.	In this case all transactions relating to partners are made directly in the Capital Accounts itself.
4.	**Can a Capital Account Show a negative balance?**	Fixed Capital Account can never show a negative balance.	Fluctuating Capital Account can show a negative balance.

Distinction Between Capital Account and Current Account :

Basis of Distinction		Capital Account	Current Account
1.	**When prepared**	It is prepared both in case of Fluctuating Capital Method as well as Fixed Capital Method.	It is prepared only in case of Fixed Capital Method.

2.	**Balance**	When Capital Account is prepared on Fixed Capital Method, it will show only Cr. Balance. In fluctuating capital Method, it may show a Cr. or a Dr. Balance.	Current Account may show a Cr. or a Dr. Balance.
3.	**Nature**	When Capital Account is prepared on Fixed Capital Method, it generally remains unchanged from year to year. In fluctuating capital method, it changes with every transaction.	Current Account Changes with every transaction.

Interest on Drawings

Interest on drawings should be calculated from the date of the withdrawal of the amount. In the absence of the date of withdrawal, interest should be charged for six months on the whole of the amount because it will be assumed that the drawings were made evenly throughout the year. For example, a partner withdrew ₹8,000 during a year and interest is to be charged at 15% per annum, interest on drawings will be calculated as follows :

$$8{,}000 \times \frac{15}{100} \times \frac{6}{12} = ₹600$$

ILLUSTRATION 4. (Fluctuating Capitals)

Shiv and Hari entered into partnership on 1st April, 2021, contributing ₹ 5,00,000 and ₹2,00,000 respectively. Hari also introduced ₹1,00,000 as additional capital on Ist July, 2021. They agreed to share profits and losses in the ratio of 3 : 2. Following information is provided regarding the partnership :

(*i*) Shiv and Hari, each are allowed a salary of ₹5,000 per quarter.

(*ii*) Interest is to be allowed on Capitals @ 8% p.a. and charged on drawings at 10% p.a.

Drawings of Shiv and Hari during the year were ₹12,000 and ₹10,000 respectively. Profit as at 31st March, 2022 before the above mentioned adjustments was ₹1,96,000.

Prepare :

(*i*) Necessary journal entries relating to appropriation of profits,

(*ii*) Profit and Loss Appropriation A/c, and

(*iii*) Partner's Capital A/cs.

SOLUTION :

Books of Shiv and Hari

JOURNAL

Date	*Particulars*	*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2022 March 31	Profit and Loss A/c Dr. To Profit and Loss Appropriation A/c (Transfer of Profit to Profit and Loss Appropriation Account)		1,96,000	1,96,000

Partner's Salary A/c Dr. To Shiv's Capital A/c To Hari's Capital A/c (Salary of partners)		40,000	 20,000 20,000
Profit and Loss Appropriation A/c Dr. To Partner's Salary A/c (Transfer of partner's salaries to Profit and Loss Appropriation Account)		40,000	 40,000
Interest on Capital A/c Dr. To Shiv's Capital A/c To Hari's Capital A/c (Interest on partner's Capitals)		62,000	 40,000 22,000
Profit and Loss Appropriation A/c Dr. To Interest on Capital A/c (Transfer of interest on Capital to Profit and Loss Appropriation Account)		62,000	 62,000
Shiv's Capital A/c Dr. Hari's Capital A/c Dr. To Interest on Drawings A/c (Interest on partner's drawings)		600 500	 1,100
Interest on Drawings A/c Dr. To Profit and Loss Appropriation A/c (Transfer of interest on drawings to Profit and Loss Appropriation Account)		1,100	 1,100
Profit and Loss Appropriation A/c Dr. To Shiv's Capital A/c To Hari's Capital A/c (Transfer of credit balance of Profit and Loss Appropriation Account to partner's Capital Accounts)		95,100	 57,060 38,040

PROFIT AND LOSS APPROPRIATION ACCOUNT
Dr. *for the year ended 31st March, 2022* Cr.

Particulars		₹	*Particulars*		₹
To Partner's Salary :			By Profit & Loss A/c		
Shiv	20,000		— being profit		1,96,000
Hari	20,000	40,000	By Interest on Drawings : (note 2)		
To Interest on Capitals : (note 1)			Shiv	600	
Shiv	40,000		Hari	500	1,100
Hari	22,000	62,000			
To Profit transferred to :					
Shiv's Capital A/c	57,060				
Hari's Capital A/c	38,040	95,100			
		1,97,100			1,97,100

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Date	Particulars	Shiv	Hari	Date	Particulars	Shiv	Hari
		₹	₹			₹	₹
2022				2021			
March 31	To Drawings	12,000	10,000	April 1	By Bank	5,00,000	2,00,000
March 31	To Interest on Drawings	600	500	July 1	By Bank	—	1,00,000
March 31	To Balance c/d	6,04,460	3,69,540	2022 March 31	By Salary	20,000	20,000
				March 31	By Interest on Capitals	40,000	22,000
				March 31	By Profit & Loss Appropriation A/c	57,060	38,040
		6,17,060	3,80,040			6,17,060	3,80,040

Note (1) : Calculation of Interest on Capitals

		₹
Shiv	On ₹5,00,000 at 8% for 1 year	40,000
Hari	On ₹2,00,000 at 8% for 1 year	16,000
	On ₹1,00,000 at 8% for 9 months	6,000
		22,000

Interest on Capitals is recorded on the debit side of P & L Appropriation A/c, as it is an item of expense for the firm. Interest on Capital is also recorded on the credit side of Capital Accounts, as it increases the Capitals.

Note (2) : In this question, the dates of drawings are not given, therefore, interest on drawings has been calculated for six months.

Hence, Interest on Shiv's drawings $= 12{,}000 \times \frac{10}{100} \times \frac{6}{12} = ₹\ 600$

Interest on Hari's drawings $= 10{,}000 \times \frac{10}{100} \times \frac{6}{12} = ₹\ 500$

Interest on Drawings is recorded on the credit side of P & L Appropriation A/c, as it is an item of income for the firm. Interest on Drawings is also recorded on debit side of Capital Accounts, as it reduces the Capitals.

Manager's Commission on Net Profits :— Sometimes, the manager is to be allowed a certain percentage of net profits as his commission. It is calculated as below:

(I) On profits before charging such commission :— For example, if the profit before charging his commission is ₹22,000 and the manager is to be allowed a commission of 10% on the profit before charging such commission, the commission will be :

$$22{,}000 \times \frac{10}{100} = ₹2{,}200.$$

(II) On profits after charging such commission :— For example, if the profit before charging his commission is ₹22,000 and the manager is to be allowed a commission of 10% on the profit after charging such commission, the commission will be :—

$$22{,}000 \times \frac{10}{110} = ₹2{,}000.$$

ILLUSTRATION 5.
(Manager's Commission)

A and *B* are partners sharing profits in the ratio of 3 : 2, with Capitals of ₹5,00,000 and ₹3,00,000 respectively. Interest on Capital is agreed @ 6% p.a. *B* is to be allowed an annual salary of ₹60,000. During the year 2019-20, the profits prior to the calculation of interest on capital but after charging *B*'s salary amounted to ₹1,80,000. A provision of 5% of the profit is to be made in respect of commission to the Manager.

Prepare Profit and Loss Appropriation account showing the distribution of profit and the partners' capital accounts for the year ending March 31, 2020.

SOLUTION :

Dr. PROFIT AND LOSS ACCOUNT Cr.
for the year ended 31st March, 2020

Particulars	₹	*Particulars*	₹
To Manager's Commission (5% of ₹2,40,000)	12,000	By Balance b/d (Profit for the year) (before *B*'s salary) (₹1,80,000 + ₹60,000)	2,40,000
To Net Profit Transferred to Profit & Loss Appropriation A/c	2,28,000		
	2,40,000		2,40,000

PROFIT AND LOSS APPROPRIATION ACCOUNT
Dr. *for the year ended on March 31, 2020* Cr.

Particulars		₹	*Particulars*	₹
To *B*'s Salary		60,000	By Profit & Loss A/c	2,28,000
To Interest on Capitals :				
A	30,000			
B	18,000	48,000		
To Profits transferred to :				
A's Capital A/c	72,000			
B's Capital A/c	48,000	1,20,000		
		2,28,000		2,28,000

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Date	*Particulars*	*A*	*B*	*Date*	*Particulars*	*A*	*B*
2020		₹	₹	2019		₹	₹
March 31	To Balance c/d	6,02,000	4,26,000	April 1	By Balance b/d	5,00,000	3,00,000
				2020			
				March 31	By Salary	—	60,000
				March 31	By Interest on Capital	30,000	18,000
				March 31	By Profit & Loss Appr. A/c (Share of profit)	72,000	48,000
		6,02,000	4,26,000			6,02,000	4,26,000

ISC Council's Instructions
In the absence of information, manager's or partner's commission will be calculated on profit before any adjustment is made according to partnership deed, *i.e.*, before adjustments in respect of partner's salary, interest on capital etc. In other words, manager's or partner's commission will be calculated on corrected Net Profit of the P & L A/c if question is silent.

Note : (1) Manager's Commission is a charge against the profits and not an appropriation of profit. Hence it is debited to Profit & Loss Account and not Profit and Loss Appropriation Account.

ILLUSTRATION 6.

A and *B* are partners in a firm sharing profits and losses in the ratio of 3 : 2 with capitals of ₹5,00,000 and ₹2,50,000 respectively on 1st April, 2018. Each partner is entitled to 10% p.a. interest on his capital. *A* is entitled to a commission of 10% on net profit remaining after deducting interest on capitals but before charging any commission. *B* is entitled to a commission of 8% of net profit remaining after deducting interest on capitals and after charging all commissions. The profits for the year ended 31st March, 2019 prior to calculation of interest on capital was ₹3,75,000.

Prepare necessary journal entries.

SOLUTION :

Books of *A* and *B*

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019 March 31	Profit and Loss A/c	Dr.		3,75,000	
	To Profit and Loss Appropriation A/c				3,75,000
	(The transfer of Profit to Profit and Loss Appropriation Account)				
"	Interest on Capital A/c	Dr.		75,000	
	To *A*'s Capital A/c				50,000
	To *B*'s Capital A/c				25,000
	(The interest on partner's Capitals)				
"	Profit and Loss Appropriation A/c	Dr.		75,000	
	To Interest on Capital A/c				75,000
	(The transfer of interest on Capital to Profit and Loss Appropriation Account)				
"	Commission A/c	Dr.		50,000	
	To *A*'s Capital A/c				30,000
	To *B*'s Capital A/c				20,000
	(Commission to partners)				
"	Profit and Loss Appropriation A/c	Dr.		50,000	
	To Commission A/c				50,000
	(The transfer of partner's commission to Profit and Loss Appropriation Account)				

"	Profit and Loss Appropriation A/c Dr. To *A*'s Capital A/c To *B*'s Capital A/c (The transfer of credit balance of Profit and Loss Appropriation Account to partner's Capital Accounts)		2,50,000	1,50,000 1,00,000

Working Notes :

PROFIT AND LOSS APPROPRIATION ACCOUNT
for the year ended 31st March, 2019

Dr. Cr.

Particulars		₹	*Particulars*	₹
To Interest on Capital			By Profit and Loss A/c	
A	50,000		— being profit	3,75,000
B	25,000	75,000		
To Commission (See Note 1)				
A	30,000			
B	20,000	50,000		
To Profit transferred to :				
A's Capital A/c	1,50,000			
B's Capital A/c	1,00,000	2,50,000		
		3,75,000		3,75,000

Note : (1) Calculation of Partner's Commission :

Profit = ₹3,75,000 – ₹75,000 = ₹3,00,000

A's Commission (before charging such commission) = $3,00,000 \times \frac{10}{100}$ = ₹30,000

B's Commission (after charging such commission) =
B's Commission will be calculated after charging *A*'s Commission and his own Commission :

Hence, *B*'s Commission = $(3,00,000 - 30,000) \times \frac{8}{108}$ = ₹20,000

ILLUSTRATION 7.

A and *B* are partners sharing profits and losses in the ratio of 2 : 1 with capitals of ₹10,00,000 and ₹5,00,000 respectively on 1st April, 2019. Each partner is entitled to 8% p.a. interest on his capital. *B* is entitled to a salary of ₹3,500 p.m. together with a commission of 10% of Net Profit remaining after deducting interest on capitals and salary and after charging his commission. The profits for the year ended 31st March, 2020 prior to calculation of interest on capital but after charging salary of *B* amounted to ₹4,50,000. Show the division of profit, pass journal entries and prepare Partner's Capital Accounts : (*i*) When capitals are fixed, and (*ii*) When capitals are fluctuating.

SOLUTION : PROFIT AND LOSS APPROPRIATION ACCOUNT
for the year ended 31st March, 2020

Dr. Cr.

Particulars	₹	*Particulars*	₹
To *B*'s Salary	42,000	By Profit and Loss A/c —	

To Interest on Capitals :		(being profit before *B*'s salary) (₹4,50,000 + ₹42,000)	4,92,000
A 80,000			
B 40,000	1,20,000		
To Commission to *B* (See Note 1)	30,000		
To Profits transferred to :			
A's Capital/ Current* A/c 2,00,000			
B's Capital/ Current* A/c 1,00,000	3,00,000		
	4,92,000		4,92,000

*Current A/c will be written in case of fixed capitals.

Note : (1) Calculation of Partner's Commission :

Profit = ₹4,50,000 – Interest on Capital ₹1,20,000 = ₹3,30,000

B's Commission (after charging such commission) = $3,30,000 \times \frac{10}{110}$ = ₹30,000

(*i*) When Capitals are fixed :

In the Books of *A* and *B*

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2020					
March 31	Profit and Loss A/c	Dr.		4,92,000	
	To Profit and Loss Appropriation A/c				4,92,000
	(Transfer of net profit to Profit and Loss Appropriation Account)				
March 31	*B*'s Salary A/c	Dr.		42,000	
	To *B*'s Current A/c				42,000
	(*B*'s salary credited to his Current Account)				
March 31	Profit and Loss Appropriation A/c	Dr.		42,000	
	To *B*'s Salary A/c				42,000
	(*B*'s Salary transferred to Profit and Loss Appropriation Account)				
March 31	Interest on Capital A/c	Dr.		1,20,000	
	To *A*'s Current A/c				80,000
	To *B*'s Current A/c				40,000
	(Interest on capital allowed to partners)				
March 31	Profit and Loss Appropriation A/c	Dr.		1,20,000	
	To Interest on Capital A/c				1,20,000
	(Interest on capital transferred to Profit and Loss Appropriation Account)				
March 31	Commission to *B*	Dr.		30,000	
	To *B*'s Current A/c				30,000
	(*B*'s Commission credited to his Current A/c)				

March 31	Profit and Loss Appropriation A/c Dr.		30,000	
	To Commission to *B*			30,000
	(*B*'s Commission transferred to Profit & Loss Appropriation Account)			
March 31	Profit and Loss Appropriation A/c Dr.		3,00,000	
	To *A*'s Current A/c			2,00,000
	To *B*'s Current A/c			1,00,000
	(Divisible profit of ₹3,00,000 credited to partner's Current Accounts in 2 : 1)			

Dr. CAPITAL ACCOUNTS Cr.

Date	Particulars	A	B	Date	Particulars	A	B
2020		₹	₹	2019		₹	₹
March 31	To Balance c/d	10,00,000	5,00,000	April 1	By Balance b/d	10,00,000	5,00,000

Dr. CURRENT ACCOUNTS Cr.

Date	Particulars	A	B	Date	Particulars	A	B
2020		₹	₹	2020		₹	₹
March 31	To Balance c/d	2,80,000	2,12,000	March 31	By Salary		42,000
				March 31	By Interest on Capitals	80,000	40,000
				March 31	By Commission		30,000
				March 31	By Profit & Loss Appropriation A/c (Share of Profit)	2,00,000	1,00,000
		2,80,000	2,12,000			2,80,000	2,12,000

(*ii*) When Capitals are fluctuating :

In the Books of *A* and *B*

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2020				
March 31	Profit and Loss A/c Dr.		4,92,000	
	To Profit and Loss Appropriation A/c			4,92,000
	(Transfer of net profit to Profit and Loss Appropriation A/c)			
,,	*B*'s Salary A/c Dr.		42,000	
	To *B*'s Capital A/c			42,000
	(*B*'s salary credited to *B*'s Capital Account)			

,,	Profit and Loss Appropriation A/c Dr. To *B*'s Salary A/c (*B*'s salary transferred to Profit and Loss Appropriation A/c)		42,000	42,000
,,	Interest on Capital A/c Dr. To *A*'s Capital A/c To *B*'s Capital A/c (Interest on Capital allowed to partners)		1,20,000	80,000 40,000
,,	Profit and Loss Appropriation A/c Dr. To Interest on Capital A/c (Interest on capital transferred to Profit and Loss Appropriation A/c)		1,20,000	1,20,000
,,	Commission to *B* Dr. To *B*'s Capital A/c (*B*'s Commission credited to his Capital A/c)		30,000	30,000
,,	Profit and Loss Appropriation A/c Dr. To Commission to *B* (*B*'s Commission transferred to Profit & Loss Appropriation A/c)		30,000	30,000
,,	Profit and Loss Appropriation A/c Dr. To *A*'s Capital A/c To *B*'s Capital A/c (Divisible profit of ₹3,00,000 credited to partner's Capital Accounts in 2 : 1)		3,00,000	2,00,000 1,00,000

Dr. CAPITAL ACCOUNTS Cr.

Date	*Particulars*	*A*	*B*	*Date*	*Particulars*	*A*	*B*
2020		₹	₹	2019		₹	₹
March 31	To Balance c/d	12,80,000	7,12,000	April 1	By Balance b/d	10,00,000	5,00,000
				2020			
				March 31	By Salary		42,000
				March 31	By Interest on Capitals	80,000	40,000
				March 31	By Commi-ssion		30,000
				March 31	By Profit and Loss Appro-priation A/c (Share of Profit)	2,00,000	1,00,000
		12,80,000	7,12,000			12,80,000	7,12,000

Note : Commission of manager is written in Profit and Loss A/c whereas commission of partner is written in Profit and Loss Appropriation A/c.

ILLUSTRATION 8.

Ram and *Gopal* were partners in a firm sharing profits in the ratio of 3 : 2. On 1st April, 2021 their fixed capitals were ₹1,00,000 and ₹1,50,000 respectively. On 30th June, 2021 they decided that their total capital (fixed) should be ₹3,00,000. It was further decided that the capital (fixed) should be in their profit sharing ratio. Accordingly they introduced or withdrew the necessary capital. The partnership deed provided the following :

(*i*) Interest on capital @ 12% p.a.

(*ii*) Interest on drawings @ 18% p.a.

(*iii*) Monthly salary to *Ram* @ ₹2,000 per month and to *Gopal* at the rate of ₹3,000 per month.

The drawings of *Ram* and *Gopal* during the year were as follows :

Date	*Ram*	*Gopal*
2021	₹	₹
Oct. 1	10,000	12,000
Dec. 31	15,000	12,000

The profit earned by the firm for the year ended 31st March, 2022 was ₹2,00,000. 10% of this profit was to be kept as a reserve.

You are required to prepare :

(*i*) Profit and Loss Appropriation Account,

(*ii*) Capital Accounts of *Ram* and *Gopal,* and

(*iii*) Current Accounts of *Ram* and *Gopal.*

SOLUTION : PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2022* Cr.

		₹			₹
To Reserve		20,000	By Profit & Loss A/c —being profit		2,00,000
To Interest on Capitals :			By Interest on Drawings :		
Ram's Current A/c	19,200		*Ram*'s Current A/c	1,575	
Gopal's Current A/c	15,300	34,500	*Gopal*'s Current A/c	1,620	3,195
To Salary					
Ram's Current A/c	24,000				
Gopal's Current A/c	36,000	60,000			
To Profit Transferred to :					
Ram's Current A/c	53,217				
Gopal's Current A/c	35,478	88,695			
		2,03,195			2,03,195

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*Ram*	*Gopal*	*Particulars*	*Ram*	*Gopal*
	₹	₹		₹	₹
To Bank A/c		30,000	By Balance b/d	1,00,000	1,50,000
To Balance c/d	1,80,000	1,20,000	By Bank A/c	80,000	
	1,80,000	1,50,000		1,80,000	1,50,000

PARTNER'S CURRENT ACCOUNTS

Dr. Cr.

Particulars	*Ram*	*Gopal*	*Particulars*	*Ram*	*Gopal*
	₹	₹		₹	₹
To Drawings	25,000	24,000	By Interest on Capital	19,200	15,300
To Interest on Drawings	1,575	1,620	By Salary	24,000	36,000
To Balance c/d	69,842	61,158	By Profit & Loss Appropriation A/c	53,217	35,478
	96,417	86,778		96,417	86,778

Working Notes :

(*i*) Calculation of New Capitals :
Ram's Capital 3/5 of ₹3,00,000 = ₹1,80,000
Gopal's Capital 2/5 of ₹3,00,000 = ₹1,20,000

(*ii*) Capital to be introduced by *Ram* = ₹1,80,000 – ₹1,00,000 = ₹80,000
Capital to be withdrawn by *Gopal* = ₹1,50,000 – ₹1,20,000 = ₹30,000

(*iii*) Calculation of Interest on Capital :

	Ram	*Gopal*
Interest for 3 months *i.e.* from 1st April 2021 to 30th June 2021 :		
Ram on ₹1,00,000 @ 12% p.a.	3,000	
Gopal on ₹1,50,000 @ 12% p.a.		4,500
Interest for 9 months i.e. from 1st July 2021 to 31st March 2022 :		
Ram on ₹1,80,000 @ 12% p.a.	16,200	
Gopal on ₹1,20,000 @ 12% p.a.		10,800
	19,200	15,300

(*iv*) Calculation of Interest on Drawings :

	Ram	*Gopal*
Interest for 6 months *i.e.* from 1st Oct. 2021 to 31st March 2022 :		
Ram on ₹10,000 @ 18% p.a.	900	
Gopal on ₹12,000 @ 18% p.a.		1,080
Interest for 3 months i.e. from 1st Jan. 2022 to 31st March 2022 :		
Ram on ₹15,000 @ 18% p.a.	675	
Gopal on ₹12,000 @ 18% p.a.		540
	1,575	1,620

Interest on Partner's Loan to the Firm :

Rate of Interest : If a partner has given loan to the firm, he is entitled to receive interest on such loan at an agreed rate of interest. However, if there is no agreement as to the rate of interest, he is entitled to receive interest on loan @ 6% per annum.

Nature of Interest : Interest on partner's loan is a charge against the profits and hence, such interest is allowed whether there are profits or not.

Accounting Treatment : It is treated as a charge against the profits and hence interest on partner's loan is debited to Profit & Loss A/c and not to Profit & Loss Appropriation A/c.

ISC Council's Instructions

Interest on partner's loan is not credited to the partner's Capital or Current Accounts. It is credited to his Loan Account.

The following entries are passed for interest on Partner's Loan :

(*i*) For providing Interest on Partner's Loan :

Interest on Partner's Loan A/c Dr.
To Partner's Loan A/c

(*ii*) For closing the Interest on Partner's Loan A/c :

Profit & Loss A/c Dr.
To Interest on Partner's Loan A/c

ILLUSTRATION 9.

A and *B* entered into partnership on 1st April, 2021 without any partnership deed. They introduced capitals of ₹5,00,000 and ₹3,00,000 respectively. On 31st October 2021, *A* advanced ₹2,00,000 by way of loan to the firm without any agreement as to interest.

The Profit and Loss Account for the year ended 31.3.2022 showed a profit of ₹4,30,000, but the partners could not agree upon the amount of interest on loan to be charged and the basis of division of profits. Pass a journal entry for the distribution of the profit between the partners and prepare the Capital A/cs of both the partners and Loan A/c of *A*.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
Mar. 31	Profit and Loss Appropriation A/c	Dr.		4,25,000	
	To *A*'s Capital A/c				2,12,500
	To *B*'s Capital A/c				2,12,500
	(Profit distributed by *A* and *B* equally)				

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Date	Particulars	*A*	*B*	Date	Particulars	*A*	*B*
2022		₹	₹	2021		₹	₹
Mar. 31	To Balance c/d	7,12,500	5,12,500	April 1	By Bank A/c	5,00,000	3,00,000
				2022			
				Mar. 31	By Profit and Loss App. A/c (Profit)	2,12,500	2,12,500
		7,12,500	5,12,500			7,12,500	5,12,500

Dr. *A*'S LOAN ACCOUNT Cr.

Date	Particulars	₹	Date	Particulars	₹
2022			2021		
Mar. 31	To Balance c/d	2,05,000	Oct. 31	By Bank A/c	2,00,000
			2022		
			Mar. 31	By Interest on Loan A/c	5,000
		2,05,000			2,05,000

Working Notes :

1. Interest on *A*'s Loan = ₹2,00,000 × $\frac{6}{100} \times \frac{5}{12}$ = ₹5,000

   Interest on Loan is to be paid @6% p.a.

2. Net Profit after interest on *A*'s Loan = ₹4,30,000 – ₹5,000 = ₹4,25,000
3. Interest on Loan is not credited to Partner's Capital A/c. It is credited to his Loan A/c.

ILLUSTRATION 10.

A and *B* are partners with capitals of ₹5,00,000 and ₹3,00,000 respectively. The profit for the year ended 31st March 2022 was ₹3,46,000 before allowing interest on partner's loan. Show the distribution of profit after taking the following into consideration:

(*i*) Interest on *A*'s Loan of ₹1,50,000 to the firm provided on 1st April 2021.
(*ii*) Interest on capital to be allowed @ 5% p.a.
(*iii*) Interest on drawings @ 6% p.a. Drawings were *A* ₹60,000 and *B* ₹40,000.
(*iv*) *B* is to be allowed a Commission of 2% on sales. Sales for the year were ₹30,00,000.
(*v*) 10% of the divisible profits is to be kept in a Reserve Account.

SOLUTION :

PROFIT AND LOSS ACCOUNT
for the year ended 31st March, 2022

Dr. Cr.

Particulars	₹	Particulars	₹
To Interest on *A*'s Loan	9,000	By Balance b/d (Profit before interest)	3,46,000
To Profit transferred to Profit & Loss Appropriation A/c	3,37,000		
	3,46,000		3,46,000

PROFIT AND LOSS APPROPRIATION ACCOUNT
for the year ended 31st March, 2022

Dr. Cr.

Particulars		₹	Particulars		₹
To Interest on Capital :			By Profit & Loss A/c — Net Profit		3,37,000
A	25,000		By Interest on Drawings :		
B	15,000	40,000	*A*	1,800	
To Commission to *B*		60,000	*B*	1,200	3,000
To Reserve A/c		24,000			
To Profit transferred to					
A's Capital A/c	1,08,000				
B's Capital A/c	1,08,000	2,16,000			
		3,40,000			3,40,000

Notes :

(1) If a partner has given loan to the firm and if the rate of interest on such loan has not been given in the question, then under the Partnership Act, interest at the rate of 6% p.a. is to be allowed on such loan.

(2) Since interest on partner's loan is treated as a charge against profit, interest on *A*'s Loan is debited to Profit & Loss Account.

(3) Since the date of drawings is not given, interest on drawings will be calculated for an average period, *i.e.*, six months.

(4) Amount transferred to Reserve has been calculated at 10% of ₹2,40,000 (*i.e.*, ₹3,37,000 + ₹3,000 – ₹40,000 – ₹60,000).

ILLUSTRATION 11.

X and *Y* are partners with a profit sharing ratio of 1 : 2 with capitals of ₹4,00,000 and ₹6,00,000 respectively. On 1st October, 2021 *X* and *Y* granted loans of ₹1,00,000 and ₹60,000 respectively to the firm. Distribute the profit/losses amongst the partners for the year ended 31st March, 2022 in each of the following cases:

Case (*a*) If the profit before interest for the year amounted to ₹12,000.

(*b*) If the profit before interest for the year amounted to ₹3,000.

(*c*) If the loss before interest for the year amounted to ₹7,500.

SOLUTION:

Case (*a*) PROFIT AND LOSS ACCOUNT

Dr. *for the year ending on 31st March, 2022* Cr.

Particulars		₹	*Particulars*	₹
To Interest on Loan :			By Balance b/d	
X	3,000		(Profit before interest)	12,000
Y	1,800	4,800		
To Net Profit transferred to				
Profit & Loss Appropriation A/c		7,200		
		12,000		12,000

PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended on 31st March, 2022* Cr.

Particulars		₹	*Particulars*	₹
To Net Profit transferred to :			By Profit & Loss A/c	
X's Capital A/c	2,400		(Profit for the year)	7,200
Y's Capital A/c	4,800	7,200		
		7,200		7,200

Case (*b*) PROFIT AND LOSS ACCOUNT

Dr. *for the year ending on 31st March, 2022* Cr.

Particulars		₹	*Particulars*		₹
To Interest on Loan :			By Balance b/d		
X	3,000		(Profit before interest)		3,000
Y	1,800	4,800	By Net Loss transferred to :		
			X's Capital A/c	600	
			Y's Capital A/c	1,200	1,800
		4,800			4,800

Case (c)

PROFIT AND LOSS ACCOUNT
for the year ending on 31st March, 2022

Dr. Cr.

Particulars		₹	*Particulars*		₹
To Balance B/d (Loss before interest)		7,500	By Net Loss transferred to :		
To Interest on Loan :			*X*'s Capital A/c	4,100	
X	3,000		*Y*'s Capital A/c	8,200	12,300
Y	1,800	4,800			
		12,300			12,300

Notes : (*i*) Interest on *X*'s Loan $= ₹1,00,000 \times \frac{6}{100} \times \frac{6}{12} = ₹3,000$

(*ii*) Interest on *Y*'s Loan $= ₹\ 60,000 \times \frac{6}{100} \times \frac{6}{12} = ₹1,800$

Interest on Loan taken by a Partner from the Firm

The Indian Partnership Act 1932 does not provide for charging interest on loan taken by a partner from the firm. Hence, interest is charged on loan to the partner if the Partnership Deed has a clause in this respect or when the partners have agreed to the rate of interest to be charged on such loan.

Nature of Interest : Interest on loan taken by a partner is a gain for the firm and is recorded on the credit side of Profit & Loss Account.

Accounting Treatment : Interest on loan taken by a partner from the firm is credited to Profit & Loss Account and debited to his Capital/Current Account.

The following entries are passed for it :

(*i*) For charging Interest on Loan to a partner :
Partner's Capital/Current A/c Dr.
To Interest on Partner's Loan A/c

(*ii*) For closing the Interest on Partner's Loan A/c :
Interest on Partner's Loan A/c Dr.
To Profit & Loss A/c

ILLUSTRATION 12.

A and *B* are partners sharing profits in the ratio of 3 : 2. On 1st April, 2021 their capitals were ₹5,00,000 and ₹3,00,000 respectively. *A* was in need of funds and hence took a loan of ₹1,00,000 from the firm on 1st July, 2021, agreed rate of interest being 12% p.a.

Profit for the year ended 31st March, 2022 amounted to ₹1,50,000 before charging interest on loan to *A*.

Pass Journal Entries for interest and prepare Partner's Capital Accounts.

SOLUTION:

JOURNAL OF *A* AND *B*

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022 March 31	*A*'s Capital A/c	Dr.		9,000	
	To Interest on *A*'s Loan A/c				9,000
	(Interest charged on Loan to *A* for nine months @ 12% p.a.)				
,,	Interest on *A*'s Loan A/c	Dr.		9,000	
	To Profit and Loss A/c				9,000
	(Transfer of Interest on Loan to P & L A/c)				

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Date	Particulars	*A*	*B*	Date	Particulars	*A*	*B*
2022		₹	₹	2021		₹	₹
March 31	To Interest on *A*'s Loan A/c	9,000		April 1	By Balance b/d	5,00,000	3,00,000
March 31	To Balance c/d	5,86,400	3,63,600	2022 March 31	By Profit & Loss Appropriation A/c	95,400	63,600
		5,95,400	3,63,600			5,95,400	3,63,600

Note :

	₹
Net Profit before Interest on *A*'s Loan	1,50,000
Add : Interest on *A*'s Loan	9,000
Divisible Profit to be divided in 3 : 2	1,59,000

CASE BASED MCQS — 1

Shruti and Vandna were partners. Their capitals as on 1st April 2021 were ₹3,00,000 and ₹2,00,000 respectively. Interest on Capital is to be allowed @ 8% p.a. as a charge.On 1st November 2021, Shruti advanced ₹2,00,000 as loan to the firm and on the same date, the firm advanced loan of ₹80,000 to Vandna. Both the loans were without an agreement.

Loss for the year ending 31st March, 2022 before allowing and charging interest on loan was ₹35,000.

Based on the above information, Choose the correct answer :

(*a*) Interest on Capital

(*i*) Will be allowed debiting Profit and Loss Appropriation A/c

(*ii*) Will be allowed debiting Profit and Loss A/c

(*iii*) Will be allowed @ 6% p.a. debiting Profit and Loss A/c

(*iv*) Will not be allowed because the firm has incurred loss during the year.

(*b*) Interest on Loan by Shruti :

(*i*) Will not be allowed because there is no agreement to allow interest.

(*ii*) Will not be allowed because there is no agreement regarding rate of interest.

(*iii*) Will not be allowed because the firm has incurred loss during the year.

(*iv*) Will be allowed @ 6% p.a.

(*c*) Interest on Loan to Vandna :

(*i*) Will be Charged @ 6% p.a. and Credited to Profit and Loss Account.

(*ii*) Will be Charged @ 6% p.a. and Credited to Profit and Loss Appropriation Account.

(*iii*) Will not be Charged.

(*iv*) Will be Charged at Bank Rate and Credited to Profit & Loss Account.

(*d*) Shruti's share of loss will be :

(*i*) ₹48,000
(*ii*) ₹40,000
(*iii*) ₹40,500
(*iv*) ₹48,600

(See Answers at the end of the book)

Rent paid to a Partner : Like interest on partner's loan, rent paid to a partner is also treated as a charge against profit and not an appropriation out of profit and hence it should be debited to Profit and Loss Account and not to Profit and Loss Appropriation Account and Credited to partner's Current Account in case of fixed capital system or to partner's Capital Account when Capitals are fluctuating.

ILLUSTRATION 13.

Rahim and Sudesh, the two partners of a business firm, agreed to appropriate the profits of their firm on the following terms :

(*a*) Interest is payable on capital @ 5% per annum.

(*b*) Rahim will be entitled to a salary of ₹500 per month.

(*c*) Loan advanced by a partner to the firm is to carry interest @ 10% per annum.

(*d*) Interest on drawings to be charged from the partners @ 5% per annum.

(*e*) Sudesh will get commission @ 1% on the sales made during the year.

(*f*) Rahim is entitled to a rent of ₹25,000 per annum for allowing the firm to carry on the business in his premises.

The net profit of the firm for the year ended 31st March, 2019, was ₹1,75,500 before taking into account any of the above terms.

Particulars	*Rahim*	*Sudesh*
	₹	₹
Capital Balances on 1st April, 2018	1,50,000	1,40,000
Loan advanced to the Firm on 1st October, 2018	—	1,00,000

Drawings made during the year	40,000	30,000
Loan taken from the firm on 1st July 2018 @ 12% p.a.	50,000	

During the year 2018-19, sales of the firm amounted to ₹7,00,000.

From the above information, prepare :

(a) Profit and Loss Appropriation Account.

(b) Partner's Capital Accounts.

SOLUTION :

PROFIT AND LOSS ACCOUNT

for the year ended 31st March, 2019

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Interest on Sudesh's Loan	5,000	By Profit before interest	1,75,500
To Rent : Rahim	25,000	By Interest on Rahim's Loan	4,500
To Profit transferred to Profit & Loss Appropriation A/c	1,50,000		
	1,80,000		1,80,000

PROFIT AND LOSS APPROPRIATION ACCOUNT

for the year ended 31st March, 2019

Dr. Cr.

Particulars		₹	*Particulars*		₹
To Interest on Capital :			By Profit & Loss A/c (Net Profit)		1,50,000
Rahim	7,500		By Interest on Drawings (for six months)		
Sudesh	7,000	14,500	Rahim	1,000	
To Salary (Rahim)		6,000	Sudesh	750	1,750
To Commission Sudesh $(7,00,000 \times \frac{1}{100})$		7,000			
To Profit transferred to :					
Rahim's Capital A/c	62,125				
Sudesh's Capital A/c	62,125	1,24,250			
		1,51,750			1,51,750

PARTNER'S CAPITAL ACCOUNTS

Dr. Cr.

Particulars	*Rahim*	*Sudesh*	*Particulars*	*Rahim*	*Sudesh*
	₹	₹		₹	₹
To Drawings	40,000	30,000	By Balance b/d	1,50,000	1,40,000
To Interest on Drawings	1,000	750	By Rent	25,000	
To Interest on Rahim's Loan	4,500		By Interest on Capital	7,500	7,000
To Balance c/d	2,05,125	1,85,375	By Salary	6,000	
			By Commission		7,000
			By Profit & Loss Appropriation A/c (Profit)	62,125	62,125
	2,50,625	2,16,125		2,50,625	2,16,125

Working Notes :

(*i*) Interest on Sudesh's Loan has been treated as a charge against profits. It has been debited to P & L A/c and will be credited to a separate Loan A/c.

(*ii*) Rent paid to a partner has also been treated as charge against profits. It is also debited to P & L A/c and has been credited to Partner's Capital Account.

(*iii*) In the absence of information about the date of drawings, interest on drawings has been calculated for six months.

CASE BASED MCQS — 2

Kanishk and Lalit are partners with fixed capitals of ₹5,00,000 and ₹10,00,000 respectively. The profit for the year ending 31st March 2022 was ₹3,30,000 before providing for any of the following adjustments :

(*i*) Kanishk is entitled to rent of ₹10,000 per month for using his property for business purpose.

(*ii*) Lalit is entitled to quarterly salary of ₹20,000.

(*iii*) Manager is to be allowed a commission of 5% of net profit after charging his commission.

Based on the above information you are required to answer the following questions :

(*a*) Rent payable to Kanishk will be :

(*i*) Credited to his Capital Account
(*ii*) Credited to his Current Account
(*iii*) Credited to Rent Payable Account
(*iv*) Debited to Profit & Loss Appropriation Account

(*b*) Salary payable to Lalit will be :

(*i*) Credited to his Capital Account
(*ii*) Credited to his Current Account
(*iii*) Debited to Profit & Loss Account
(*iv*) Credited to Profit & Loss Appropriation Account

(*c*) Net Profit for the year will be

(*i*) ₹2,10,000 (*ii*) ₹2,00,000
(*iii*) ₹1,40,000 (*iv*) ₹3,30,000

(*d*) Kanishk's share of profit will be :

(*i*) ₹40,000 (*ii*) ₹80,000
(*iii*) ₹90,000 (*iv*) ₹60,000

(See Answers at the end of the book)

CASE BASED MCQs — 3

On 1st September 2020, twenty students of Modern College started their Partnership Firm in the name of "Be Safe" for selling sanitisers on digital mode. Since they were good friends of each other, they were not having any explicit agreement in place. All of them have agreed to invest ₹15,000 each as capital. The books were closed on 31st March 2021, on which date the following information was provided by the firm :

Particulars	Amount
	₹
Sale of Sanitisers	1,20,000
Cost of goods sold	50,000
Total Remuneration to partners	2,000 per month
Rent to a partner	1,000 per month
Manager's Commission	5,000
Closing Stock as on March 31,2021	9,000
6% Fixed Deposit (made on 31.3.2021)	20,000

(*a*) Calculate the amount of profits to be transferred to Profit and Loss Appropriation Account.

(*i*) Profit ₹58,000 (*ii*) Profit ₹34,000

(*iii*) Profit ₹57,200 (*iv*) Profit ₹33,200

(*b*) On 31st March 2021, Remuneration to Partners will be provided to the partners of "Be Safe" but only out of :

(*i*) Profits for the accounting year (*ii*) Reserves

(*iii*) Accumulated Profits (*iv*) Goodwill

(*c*) On 01st December 2020 one of the partners of the firm introduced additional capital of ₹30,000 and also advanced a loan of ₹40,000 to the firm. Calculate the amount of interest that Partner will receive for the current accounting period :

(*i*) ₹4,200 (*ii*) ₹1,400

(*iii*) ₹1,575 (*iv*) ₹ 800

(C.B.S.E. Sample Paper, 2021)

(See Answer at the end of the book)

When Appropriations are more than Profits :

In case where appropriations such as interest on capital, salary of partners etc. are more than available profits, the profits will be distributed in the ratio of appropriations.

ILLUSTRATION 14.

A and *B* are partners sharing profits and losses in the ratio of 2 : 1. *A* is a non-working partner and has contributed ₹12,00,000 as his capital. *B* is a working partner. The partnership deed provides for interest on capital @ 10% p.a. and salary of ₹7,500 per month to the working partner. The net profit for the year ended 31st March, 2022 before providing for interest on capital and salary amounted to ₹70,000. You are required to show the distribution of profit.

SOLUTION: PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2022* Cr.

Particulars	₹	Particulars	₹
To Interest on *A*'s Capital (4/7 of 70,000)	40,000	By Profit & Loss A/c (Net Profit)	70,000
To Salary to *B* (3/7 of 70,000)	30,000		
	70,000		70,000

Working Note :

		₹
Interest on *A*'s Capital	= 10% on ₹12,00,000	1,20,000
Salary of *B*	= ₹7,500 × 12	90,000
		2,10,000

Since available profit is only ₹70,000 which is less than appropriations of ₹2,10,000, profit will be distributed in the ratio of appropriations to be made :

	Interest on Capital	:	Salary
Or	1,20,000	:	90,000
Or	4	:	3

ILLUSTRATION 15.

Shreya and *Vivek* were partners in a firm sharing profits in the ratio 3 : 2. The balances in their capital and current accounts as on 1st April, 2017 were as under :

	Sherya (₹)	*Vivek* (₹)
Capital Accounts	5,00,000	2,50,000
Current Accounts	1,00,000 (Cr.)	28,000 (Dr.)

The partnership deed provided that *Shreya* was to be paid a salary of ₹5,000 p.m. whereas *Vivek* was to get a commission of ₹30,000 for the year.

Interest on capital was to be allowed @ 8% p.a. whereas interest on drawings was to be charged @ 6% p.a. The drawings of *Shreya* were ₹15,000 drawn on 30th September 2017 while *Vivek* withdrew ₹30,000 on 1st September, 2017. The net profit of the firm for the year before making the above adjustments was ₹1,20,000.

Prepare Profit and Loss Appropriation Account and Partner's Capital and Current Accounts. *(C.B.S.E. 2019, Chennai, Modified)*

SOLUTION : PROFIT AND LOSS APPROPRIATION A/C

for the year ended 31st March, 2018

Dr. Cr.

Particulars		*Amount*	*Particulars*		*Amount*
		₹			₹
To Partner's Current A/cs			By Profit & Loss A/c (Net Profit)		1,20,000
Shreya	81,000		By Interest on Drawings		
Vivek	40,500	1,21,500	*Shreya*	450	
			Vivek	1,050	1,500
		1,21,500			1,21,500

PARTNER'S CAPITAL A/CS

Dr. Cr.

Date	*Particulars*	*Shreya*	*Vivek*	*Date*	*Particulars*	*Shreya*	*Vivek*
2018		₹	₹	2017		₹	₹
Mar. 31	To Balance c/d	5,00,000	2,50,000	April 1	By Balance b/d	5,00,000	2,50,000
		5,00,000	2,50,000			5,00,000	2,50,000

PARTNER'S CURRENT A/CS

Dr. Cr.

Date	*Particulars*	*Shreya*	*Vivek*	*Date*	*Particulars*	*Shreya*	*Vivek*
2017		₹	₹	2017		₹	₹
April 1	To Balance b/d	—	28,000	April 1	By Balance b/d	1,00,000	—

2018 Mar. 31	To Drawings A/c	15,000	30,000	2018 Mar. 31	By P & L Appropriation A/c	81,000	40,500
Mar. 31	To Interest on Drawings	450	1,050	Mar. 31	By Balance c/d	—	18,550
Mar. 31	To Balance c/d	1,65,550					
		1,81,000	59,050			1,81,000	59,050

Working Notes :

(1) Interest on Drawings :

Shreya : $15,000 \times \frac{6}{100} \times \frac{6}{12} =$ ₹ 450

Vivek : $30,000 \times \frac{6}{100} \times \frac{7}{12} =$ ₹1,050

(2) Appropriations :

Particulars	*Shreya*	*Vivek*
	₹	₹
Interest on Capital	40,000	20,000
Salary	60,000	—
Commission	—	30,000
Amount to be paid	1,00,000	50,000

Total amount to be paid = ₹1,00,000 + ₹50,000 = ₹1,50,000

Since profits available are ₹1,20,000 + ₹1,500 = ₹1,21,500 which is less than appropriations of ₹1,50,000, appropriations will be made to the extent of ₹1,21,500 only in the ratio of 1,00,000 : 50,000 or 2 : 1.

Shreya's share $= 1,21,500 \times \frac{2}{3} =$ ₹81,000

Vivek's share $= 1,21,500 \times \frac{1}{3} =$ ₹40,500

CASE BASED MCQS — 4

Mukesh and Navdeep are partners sharing profits in 2 : 1 with capitals of ₹6,00,000 and ₹4,00,000 respectively. As per their partnership deed :

(*i*) Navdeep is entitled to a rent of ₹48,000 per year for using his property by the firm.

(*ii*) They are entitled to interest on capital @ 8% p.a.

(*iii*) Manager is allowed a commission of 10% on net profit before charging such commission.

Profit for the year ending 31st March, 2022 before any of the above adjustments amounted to ₹1,25,000.

Answer the following questions on the basis of above :

(*a*) Rent payable to Navdeep will be :

(*i*) Credited to Navdeep's Current Account

(*ii*) Credited to Navdeep's Capital Account

(*iii*) Debited to Profit & Loss Account

(*iv*) Debited to Profit & Loss Appropriation Account

(*b*) Net Profit for the year will be :

(*i*) ₹77,000 (*ii*) ₹ 69,300
(*iii*) ₹70,000 (*iv*) ₹1,25,000

(*c*) Interest on capital will be :

(*i*) Mukesh ₹46,200 and Navdeep ₹23,100
(*ii*) Mukesh ₹48,000 and Navdeep ₹32,000
(*iii*) Mukesh ₹42,000 and Navdeep ₹28,000
(*iv*) Mukesh ₹41,580 and Navdeep ₹27,720

(*d*) Divisible Profit for the year will be :

(*i*) ₹69,300 (*ii*) Nil
(*iii*) ₹70,000 (*iv*) ₹80,000

(See Answers at the end of the book)

Methods of Calculating Interest on Drawings :— Interest on drawings may be calculated from any of the two methods discussed as below :—

(1) **Simple Method :—** Under this method, interest on drawing is calculated separately on each amount of drawing, from the date of drawing till the close of accounting period. Interest on each amount of drawing is calculated with the help of the following formula :

$$\text{Interest on Drawings} = \text{Amount of Drawings} \times \frac{\text{Rate of Interest}}{100} \times \frac{\text{Months}}{12}$$

(2) **Product Method :—** Under this method, first of all the products are computed by multiplying the each set of drawings from its duration. Thereafter, the different products are added and the interest is calculated on the total of products so arrived at for one month. The advantage of this system is that separate calculations are not required each time. Following formula is used for the calculation of interest under this method :—

$$\text{Interest on Drawings} = \text{Total of products} \times \frac{\text{Rate of Interest}}{100} \times \frac{1}{12}$$

ILLUSTRATION 16.

Charu is a partner in a firm. She withdrew the following amounts during the year ended on 31st March, 2022 :—

		₹
May	1	20,000
July	31	10,000
September	30	30,000
November	30	40,000
January	1	20,000
March	31	25,000

Interest on drawings is to be charged @ 9% p.a. Calculate interest on drawings.

SOLUTION : (i) SIMPLE METHOD

Date		Amount ₹	Period (Months upto March 31)	Interest @ 9% ₹
May	1	20,000	11	1,650
July	31	10,000	8	600
September	30	30,000	6	1,350
November	30	40,000	4	1,200
January	1	20,000	3	450
March	31	25,000	0	0
		1,45,000		5,250

(ii) PRODUCT METHOD

Date		Amount ₹	Period (Months upto March 31)	Products
May	1	20,000	11	2,20,000
July	31	10,000	8	80,000
September	30	30,000	6	1,80,000
November	30	40,000	4	1,60,000
January	1	20,000	3	60,000
March	31	25,000	0	0
		1,45,000		7,00,000

$$\text{Interest} = \text{Total of Products} \times \frac{9}{100} \times \frac{1}{12} = 7{,}00{,}000 \times \frac{9}{100} \times \frac{1}{12} = ₹5{,}250$$

Interest on Monthly Drawings

When a partner makes monthly drawings, the interest may be calculated as follows :

Case (1) When drawings are made in the beginning of every month :— When drawings are made on the 1st day of every month, the amount of drawing is multiplied by the number of remaining months in that year. For example,

If the financial year closes on 31st March 2022 :

the drawing on 1st April, 2021 will be multiplied by 12,

the drawing on 1st May, 2021 will be multiplied by 11,

the drawing on 1st June, 2021 will be multiplied by 10 and so on.

The products are totalled in the end and the interest for one month is calculated on the total of products. Alternatively, if the drawings of **equal amount** are made on the 1st day of each month, the interest for $6\frac{1}{2}$ months may be calculated on the amount of total drawings for the whole year.

It is based on average period calculated as per the following formula :

$$\text{Average Period} = \frac{\text{Time left after first drawing} + \text{Time left after last drawing}}{2}$$

$$= \frac{12 \text{ months} + 1 \text{ month}}{2} = 6\frac{1}{2} \text{ months.}$$

This interest for $6\frac{1}{2}$ months will be equal to the interest on drawings calculated on monthly basis.

Note : Average period should be used only when :
(*a*) All amounts of drawings are equal, and
(*b*) The time gap between drawings is equal.

Case (2) When drawings are made at the end of every month :— When drawings are made on the last day of every month, the interest on drawings will be calculated as below :

If the financial year closes on 31st March 2022 :

Drawings on 30th April, 2021 will be multiplied by 11

Drawings on 31st May, 2021 will be multiplied by 10

Drawings on 30th June, 2021 will be multiplied by 9 and so on.

The products are totalled in the end and the interest for one month is calculated on the total of products. Alternatively, if the drawings of **equal amount** are made on the last day of each month, the interest for $5\frac{1}{2}$ months may be calculated on the amount of total drawings for the whole year.

It is also based on the above mentioned formula :—

$$\text{Average Period} = \frac{\text{Time left after first drawing} + \text{Time left after last drawing}}{2}$$

$$= \frac{11 \text{ months} + 0 \text{ month}}{2} = 5\frac{1}{2} \text{ months.}$$

This interest for $5\frac{1}{2}$ months will be equal to the interest on drawings calculated on monthly basis.

Case (3) When drawings are made in the middle or at any time during the month, interest on the whole amount will be calculated for 6 months.

ILLUSTRATION 17.

A, *B* and *C* are partners in a firm. You are informed that :

(*i*) *A* draws ₹10,000 from the firm in the beginning of every month,

(*ii*) *B* draws ₹10,000 from the firm at the end of every month, and

(*iii*) *C* draws ₹10,000 from the firm in the middle of every month.

Interest on drawings is to be charged @ 8% p.a. Calculate interest on partner's drawings.

SOLUTION :

When drawings of equal amount are made at regular intervals, interest will be calculated for average period. Average Period will be calculated as per the following formula :

$$\text{Average Period} = \frac{\text{Time left after first drawing + Time left after last drawing}}{2}$$

(*i*) If drawings of a regular amount are made in the beginning of every month :

$$\text{Average Period} = \frac{\text{12 months + 1 month}}{2} = 6\frac{1}{2}\text{ months}$$

Interest on the whole amount will be calculated for $6\frac{1}{2}$ months :

$$\text{Interest} = 1{,}20{,}000 \times \frac{8}{100} \times \frac{6.5}{12} = ₹5{,}200$$

(*ii*) If drawings of a regular amount are made at the end of every month :

$$\text{Average Period} = \frac{\text{11 months + 0 month}}{2} = 5\frac{1}{2}\text{ months}$$

Interest on the whole amount will be calculated for $5\frac{1}{2}$ months :

$$\text{Interest} = 1{,}20{,}000 \times \frac{8}{100} \times \frac{5.5}{12} = ₹4{,}400$$

(*iii*) If drawings are made in the middle or at any time during the month :

$$\text{Average Period} = \frac{\text{11.5 months + 0.5 month}}{2} = \text{6 months}$$

Interest on the whole amount will be calculated for 6 months :

$$\text{Interest} = 1{,}20{,}000 \times \frac{8}{100} \times \frac{6}{12} = ₹4{,}800.$$

Case (4) When drawings of equal amount are made in the beginning of each quarter :

$$\text{Average Period} = \frac{\text{Time left after first drawing + Time left after last drawing}}{2}$$

$$= \frac{\text{12 months + 3 months}}{2} = 7\frac{1}{2}\text{ months.}$$

Interest on the whole amount of drawings will be charged for $7\frac{1}{2}$ months.

Note : Quarter means three months.

Case (5) When drawings of equal amount are made at the end of each quarter :

$$\text{Average Period} = \frac{\text{Time left after first drawing + Time left after last drawing}}{2}$$

$$= \frac{\text{9 months + 0 month}}{2} = 4\frac{1}{2}\text{ months.}$$

Interest on the whole amount of drawings will be charged for $4\frac{1}{2}$ months.

Case (6) When drawings of equal amount are made during the middle of each quarter :

$$\text{Average Period} = \frac{\text{Time left after first drawing + Time left after last drawing}}{2}$$

$$= \frac{10.5 \text{ months} + 1.5 \text{ months}}{2} = 6 \text{ months.}$$

Interest on the whole amount of drawings will be charged for 6 months.

ILLUSTRATION 18.

Calculate the interest on drawings of Mr. Navdeep @ 10% p.a. for the year ended 31st March, 2022 in each of the following alternative cases :

Case (*a*) If he withdrew ₹20,000 in the beginning of each quarter.
Case (*b*) If he withdrew ₹20,000 at the end of each quarter.
Case (*c*) If he withdrew ₹20,000 during the middle of each quarter.

SOLUTION :

Total drawings for the year = ₹20,000 × 4 times in a year = ₹80,000

$$\text{Average Period} = \frac{\text{Time left after first drawing + Time left after last drawing}}{2}$$

Case (*a*) Average Period $= \frac{12 \text{ months} + 3 \text{ months}}{2} = 7.5$ months.

Interest on Drawings $= ₹80{,}000 \times \frac{10}{100} \times \frac{7.5}{12} = ₹5{,}000$

Case (*b*) Average Period $= \frac{9 \text{ months} + 0 \text{ month}}{2} = 4.5$ months.

Interest on Drawings $= ₹80{,}000 \times \frac{10}{100} \times \frac{4.5}{12} = ₹3{,}000$

Case (*c*) Average Period $= \frac{10.5 \text{ months} + 1.5 \text{ months}}{2} = 6$ months.

Interest on Drawings $= ₹80{,}000 \times \frac{10}{100} \times \frac{6}{12} = ₹4{,}000$

ILLUSTRATION 19.

Calculate the interest on drawings of Mr. Arun @ 10% p.a. for the year ended 31st March, 2022 in each of the following alternative cases :

Case (*a*) If he withdrew ₹5,000 p.m. in the beginning of every month;
Case (*b*) If he withdrew ₹5,000 p.m. at the end of every month;
Case (*c*) If he withdrew ₹5,000 p.m. during the year;
Case (*d*) If he withdrew ₹60,000 during the year;
Case (*e*) If he withdrew as follows :

	₹
1st June, 2021	20,000
31st August, 2021	10,000
31st Oct., 2021	18,000
1st Feb., 2022	12,000

Case (*f*) If he withdrew ₹15,000 in the beginning of each quarter;

Case (*g*) If he withdrew ₹15,000 at the end of each quarter;

Case (*h*) If he withdrew ₹15,000 during the middle of each quarter.

SOLUTION :

Case (*a*) Average Period $= \frac{12 \text{ months} + 1 \text{ month}}{2} = 6\frac{1}{2}$ months.

Interest on Drawings $= ₹60{,}000 \times \frac{10}{100} \times \frac{6.5}{12} = ₹3{,}250$

Case (*b*) Average Period $= \frac{11 \text{ months} + 0 \text{ month}}{2} = 5\frac{1}{2}$ months.

Interest on Drawings $= ₹60{,}000 \times \frac{10}{100} \times \frac{5.5}{12} = ₹2{,}750$

Case (*c*) Assuming that the drawings were made in the middle of every month :

Average Period $= \frac{11.5 \text{ months} + 0.5 \text{ month}}{2} = 6$ months.

Interest on Drawings $= ₹60{,}000 \times \frac{10}{100} \times \frac{6}{12} = ₹3{,}000$

Case (*d*) As the date of drawing is not given, interest will be calculated for an average period of 6 months.

Interest on Drawings $= ₹60{,}000 \times \frac{10}{100} \times \frac{6}{12} = ₹3{,}000$

Case (*e*)

Date	Amount of Drawing	Period (months upto 31st March, 2022	Products
	₹		₹
1st June, 2021	20,000	10	2,00,000
31st August, 2021	10,000	7	70,000
31st Oct., 2021	18,000	5	90,000
1st Feb., 2022	12,000	2	24,000
			3,84,000

Interest on Drawings $= ₹3{,}84{,}000 \times \frac{10}{100} \times \frac{1}{12} = ₹3{,}200$

Case (*f*) Average Period $= \frac{12 \text{ months} + 3 \text{ months}}{2} = 7\frac{1}{2}$ months.

Total Drawings for the year = ₹15,000 × 4 times in a year = ₹60,000

Interest on Drawings $= ₹60{,}000 \times \frac{10}{100} \times \frac{7.5}{12} = ₹3{,}750$

Case (*g*) Average Period $= \frac{9 \text{ months} + 0 \text{ month}}{2} = 4\frac{1}{2}$ months.

Interest on Drawings $= ₹60{,}000 \times \frac{10}{100} \times \frac{4.5}{12} = ₹2{,}250$

Case (*h*) Average Period $= \dfrac{10.5 \text{ months} + 1.5 \text{ months}}{2} = 6$ months.

Interest on Drawings $= ₹60{,}000 \times \dfrac{10}{100} \times \dfrac{6}{12} = ₹3{,}000$

Case (7) When drawings of equal amount are made only during a period of 6 months ending 31st March :

(*i*) In the beginning of each month :

Average Period $= \dfrac{6 \text{ months} + 1 \text{ month}}{2} = 3\dfrac{1}{2}$ months.

Interest will be charged for $3\frac{1}{2}$ months.

(*ii*) At the end of each month :

Average Period $= \dfrac{5 \text{ months} + 0 \text{ month}}{2} = 2\dfrac{1}{2}$ months.

Interest will be charged for $2\frac{1}{2}$ months.

(*iii*) In the middle of each month :

Average Period $= \dfrac{5.5 \text{ months} + 0.5 \text{ month}}{2} = 3$ months.

ILLUSTRATION 20.

(When drawings are made only for last 6 months)

P, *Q* and *R* are partners in a firm. You find that :

(*i*) *P* drew ₹6,000 in the beginning of every month for 6 months ending 31st March, 2022.

(*ii*) *Q* drew ₹6,000 at the end of every month for 6 months ending 31st March, 2022.

(*iii*) *R* drew ₹6,000 in the middle of every month for 6 months ending 31st March, 2022.

Calculate interest on drawings @ 8% p.a.

SOLUTION :

Total drawings in all cases = ₹6,000 × 6 months = ₹36,000

	P	*Q*	*R*
Average Period	$= \frac{6+1}{2} = 3.5$ months	$\frac{5+0}{2} = 2.5$ months	$\frac{5.5+0.5}{2} = 3$ months
Interest on Drawings	$= ₹36{,}000 \times \frac{8}{100} \times \frac{3.5}{12}$ $= ₹840$	$= ₹36{,}000 \times \frac{8}{100} \times \frac{2.5}{12}$ $= ₹600$	$= ₹36{,}000 \times \frac{8}{100} \times \frac{3}{12}$ $= ₹720$

Case (8) When drawings of equal amount are made during 9 months ending 31st March :

ILLUSTRATION 21.

A, B and *C* started business on 1st July, 2021. You find that :

(*i*) *A* drew ₹8,000 in the beginning of every month for 9 months ending 31st March, 2022.

(*ii*) *B* drew ₹8,000 at the end of every month for 9 months ending 31st March, 2022.

(*iii*) *C* drew ₹8,000 every month for 9 months ending 31st March, 2022.

Calculate interest on drawings @ 10% p.a.

SOLUTION :

Total drawings in all cases = ₹8,000 × 9 months = ₹72,000

	A	*B*	*C*
Average Period	$= \frac{9+1}{2}$ = 5 months	$\frac{8+0}{2}$ = 4 months	$\frac{8.5+0.5}{2}$ = 4.5 months
Interest on Drawings	= ₹72,000 × $\frac{10}{100} \times \frac{5}{12}$ = ₹3,000	= ₹72,000 × $\frac{10}{100} \times \frac{4}{12}$ = ₹2,400	= ₹72,000 × $\frac{10}{100} \times \frac{4.5}{12}$ = ₹2,700

Case (9) When the rate of interest is given without the word 'per annum' interest will be charged without considering time or date of drawing. In other words, interest will be charged for 12 months.

ILLUSTRATION 22.

The Capital Accounts of *X* and *Y* showed balances of ₹40,000 and ₹20,000 on 1st April, 2021. They shared profits in the ratio of 3 : 2. They are allowed interest on Capitals @ 10% p.a. and are charged interest on drawings @ 12% p.a. *X* also advanced a loan of ₹10,000 to the firm on 1st August, 2021.

During the year *X* withdrew ₹1,000 per month at the beginning of every month, whereas *Y* withdrew ₹1,000 per month at the end of every month.

The profits for the year ended 31st March, 2022 before the above mentioned adjustments were ₹20,960. Show the distribution of profits and prepare the partners' Capital Accounts.

SOLUTION : PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2022* Cr.

Particulars		₹	*Particulars*		₹
To Interest on Capital :			By Profit & Loss A/c		
X	4,000		Being Profit	20,960	
Y	2,000	6,000	*Less* : Interest on *X*'s		
To Profits transferred to :			Loan @ 6% p.a.		
X's Capital A/c	9,600		for 8 months	400[1]	20,560

Y's Capital A/c	6,400	16,000	By Interest on Drawings :		
			X	780(3)	
			Y	660(4)	1,440
		22,000			22,000

Dr. CAPITAL ACCOUNTS Cr.

Date	Particulars	X	Y	Date	Particulars	X	Y
2022		₹	₹	2021		₹	₹
March 31	To Drawings	12,000	12,000	April 1	By Balance b/d	40,000	20,000
				2022			
March 31	To Interest on Drawings	780	660	March 31	By Interest on Capital	4,000	2,000
March 31	To Balance c/d	40,820	15,740	March 31	By Profit and Loss Appropriation A/c	9,600	6,400
		53,600	28,400			53,600	28,400

Notes :

(1) If a partner has given loan to the firm and if the rate of interest on such loan has not been given in the question, then under the Partnership Act, interest at the rate of 6% p.a. is to be allowed on such loan.

(2) The amount of partner's loan and the interest on loan is not recorded in the Capital Account of that partner. Interest on partner's loan is credited to a separate 'Accrued Interest Account'.

(3) Interest on X's drawings will be calculated as under :

Date of withdrawals	Amount (₹)	×	Months	=	Products
1st April, 2021	1,000		12	=	12,000
1st May, 2021	1,000		11	=	11,000
1st June, 2021	1,000		10	=	10,000
1st July, 2021	1,000		9	=	9,000
1st August, 2021	1,000		8	=	8,000
1st September, 2021	1,000		7	=	7,000
1st October, 2021	1,000		6	=	6,000
1st November, 2021	1,000		5	=	5,000
1st December, 2021	1,000		4	=	4,000
1st January, 2022	1,000		3	=	3,000
1st February, 2022	1,000		2	=	2,000
1st March, 2022	1,000		1	=	1,000
	12,000				78,000

Interest on drawings $= 78,000 \times \frac{12}{100} \times \frac{1}{12} = ₹780.$

Alternative method : (By computing for $6\frac{1}{2}$ months) :—

Interest on drawings $= 12,000 \times \frac{12}{100} \times \frac{6.5}{12} = ₹780.$

(4) Interest on Y's drawings will be calculated as under :—

Date of withdrawals	Amount (₹)	×	Months	=	Products
30th April, 2021	1,000		11	=	11,000
31st May, 2021	1,000		10	=	10,000
30th June, 2021	1,000		9	=	9,000
31st July, 2021	1,000		8	=	8,000
31st August, 2021	1,000		7	=	7,000
30th September, 2021	1,000		6	=	6,000
31st October, 2021	1,000		5	=	5,000
30th November, 2021	1,000		4	=	4,000
31st December, 2021	1,000		3	=	3,000
31st January, 2022	1,000		2	=	2,000
28th February, 2022	1,000		1	=	1,000
31st March, 2022	1,000		0	=	0
	12,000				66,000

Interest on Drawings $= 66{,}000 \times \frac{12}{100} \times \frac{1}{12} =$ ₹ 660.

Alternative method : (By computing for $5\frac{1}{2}$ months) :—

Interest on Drawings $= 12{,}000 \times \frac{12}{100} \times \frac{5.5}{12} =$ ₹ 660.

CASE BASED MCQS — 5

Shashi and Trisha were partners with fixed capitals of ₹5,00,000 and ₹3,00,000 on 1st April 2020. They are allowed interest on Capitals @ 6% p.a. and are charged interest on drawings @ 9% p.a.

During the year Shashi withdrew ₹6,000 per month in the beginning of every month, whereas Trisha withdrew ₹6,000 per quarter in the beginning of every quarter.

The profits for the year before above mentioned adjustments were ₹1,20,440.

(*a*) Interest on Trisha's Drawings will amount to :

(*i*) ₹2,430 (*ii*) ₹3,240
(*iii*) ₹4,050 (*iv*) ₹3,510

(*b*) Interest on Capital will be recorded :

(*i*) On the Credit Side of Capital Accounts
(*ii*) On the Credit Side of Profit & Loss Appropriation Account
(*iii*) On the Credit Side of Current Accounts
(*iv*) On the Debit Side of Current Accounts

(*c*) Shashi's Share of Profit will be :

(*i*) ₹50,000 (*ii*) ₹60,220
(*iii*) ₹30,000 (*iv*) ₹40,000

(*d*) Shashi's Current Account balance will be :

(*i*) Dr. 5,510 (*ii*) Cr. 5,510
(*iii*) Dr. 4,970 (*iv*) Cr. 4,970

(e) Interest on Drawings will be recorded

(i) On the Debit side of Profit & Loss Appropriation Account

(ii) On the Credit side of Current Accounts

(iii) On the Debit side of Capital Accounts

(iv) On the Credit side of Profit & Loss Appropriation Account

(See Answers at the end of the book)

CASE BASED MCQS — 6

On 1st April, 2020, Pixie, Nixie and Gypsy entered into a partnership with fixed capitals of ₹60,000, ₹50,000 and ₹30,000 respectively.

On 1st October, 2020, Pixie gave a loan of ₹12,000 to the firm.

The partnership deed contained the following clauses:

(a) Interest on drawings to be charged @ 4% per annum.

(b) Pixie to be entitled to a rent of ₹2,000 per annum for allowing the firm to carry on the business in his premises.

Nixie withdrew ₹1,000 at the end of the month for the first six months.

Net Profit of the firm for the year ending 31st March 2021 (before any interest but after rent on Pixie's premises) was ₹1,21,000.

(a) The Net Profit of the firm will be :

(i) ₹1,21,000 (ii) ₹1,20,640

(iii) ₹1,18,640 (iv) ₹ 96,640

(b) Interest on Drawings charged from Nixie will be:

(i) ₹340 (ii) ₹220

(iii) ₹170 (iv) ₹ 18.33

(I.S.C. Sample Paper, 2021)

(See Answers at the end of the book)

ILLUSTRATION 23.

A, B and *C* are in partnership. On 1st April, 2019 their capitals were : *A* ₹5,00,000 (Credit), *B* ₹3,00,000 (Credit) and *C* ₹40,000 (Debit). As per partnership deed Interest on Capital is to be allowed @ 6% p.a. and Interest on drawings is to be charged @ 8% p.a.

You find that :

(i) On 1st July 2019, *A* withdrew ₹1,00,000 against capital;

(ii) *B* withdrew ₹5,000 p.m. during the year.

(iii) *C* withdrew ₹60,000 during the year.

The profit for the year ended 31st March, 2020 amounted to ₹3,84,000.

You are required to prepare journal entries for the above transactions and also prepare partner's capital accounts.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019 July 1	*A*'s Capital A/c	Dr.		1,00,000	
	To Bank A/c				1,00,000
	(Withdrawal by *A* out of Capital)				
2020 March 31	*B*'s Capital A/c	Dr.		60,000	
	C's Capital A/c	Dr.		60,000	
	To *B*'s Drawings A/c				60,000
	To *C*'s Drawings A/c				60,000
	(Transfer of Drawings to Capital Accounts)				
March 31	Profit and Loss A/c	Dr.		3,84,000	
	To Profit and Loss Appropriation A/c				3,84,000
	(The transfer of profit to Profit and Loss Appropriation A/c)				
March 31	Interest on Capital A/c	Dr.		43,500	
	To *A*'s Capital A/c				25,500
	To *B*'s Capital A/c				18,000
	(Interest on partner's capitals)				
March 31	Profit and Loss Appropriation A/c	Dr.		43,500	
	To Interest on Capital A/c				43,500
	(Transfer of interest on Capital to Profit and Loss App. A/c)				
March 31	*B*'s Capital A/c	Dr.		2,400	
	C's Capital A/c	Dr.		2,400	
	To Interest on Drawings A/c				4,800
	(Interest on partner's drawings)				
March 31	Interest on Drawings A/c	Dr.		4,800	
	To Profit and Loss Appropriation A/c				4,800
	(Transfer of interest on drawings to Profit and Loss App. A/c)				
March 31	Profit and Loss Appropriation A/c	Dr.		3,45,300	
	To *A*'s Capital A/c				1,15,100
	To *B*'s Capital A/c				1,15,100
	To *C*'s Capital A/c				1,15,100
	(Transfer of profit to capital accounts)				

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Date	Particulars	A	B	C	Date	Particulars	A	B	C
2019		₹	₹	₹	2019		₹	₹	₹
April 1	To Bal. b/d			40,000	April 1	By Bal. b/d	5,00,000	3,00,000	

July 1	To Bank A/c	1,00,000			2020 Mar.31	By Int. on capital A/c	25,500	18,000	
2020 Mar.31	To Drawings A/c		60,000	60,000	"	By P & L App. A/c	1,15,100	1,15,100	1,15,100
"	To Interest on Drawings A/c		2,400	2,400					
"	To Bal. c/d	5,40,600	3,70,700	12,700					
		6,40,600	4,33,100	1,15,100			6,40,600	4,33,100	1,15,100

Working Notes :

(1) Interest on A's Capital : ₹

On ₹5,00,000 for 3 months : $5{,}00{,}000 \times \frac{6}{100} \times \frac{3}{12}$ = 7,500

On ₹4,00,000 for 9 months : $4{,}00{,}000 \times \frac{6}{100} \times \frac{9}{12}$ = 18,000

25,500

(2) Interest on drawings :

B's Drawings : ₹5,000 × 12 = ₹$60{,}000 \times \frac{8}{100} \times \frac{6}{12}$ = 2,400

C's Drawings : ₹$60{,}000 \times \frac{8}{100} \times \frac{6}{12}$ = 2,400

Note : In the absence of actual dates of drawings, interest thereon has been calculated for the average period *i.e.*, 6 months.

(3) Divisible Profit = ₹3,84,000 – Interest on Capital ₹43,500 + Interest on Drawings ₹4,800 = ₹3,45,300.

Each Partner's share = ₹3,45,300 ÷ 3 = ₹1,15,100.

ILLUSTRATION 24.

On 1st April, 2019, *A*, *B* and *C* started a business with capitals of ₹5,00,000, ₹4,50,000 and ₹2,50,000 respectively. According to partnership agreement :

(*i*) Profit earned in any year will be distributed as under :
Upto ₹3,00,000 equally.
Excess over ₹3,00,000 – 1/5th to *A*, 2/5th to *B* and 2/5 to *C*.

(*ii*) Allow interest on capital @5% p.a. and charge interest on drawings @8% p.a.

(*iii*) *A* and *C* are entitled to get monthly salaries of ₹4,500 and ₹5,500 respectively. In addition to salaries, both are entitled to get a commission of 4% (each) on net profit after taking into consideration salaries, interest and all commissions.

Drawings of the partners during the year were :

A withdrew regularly ₹9,000 at the end of every month.

B withdrew regularly ₹8,000 at the beginning of every month.

C withdrew ₹50,000 during the year.

The profit of the firm for the year before charging all of the above adjustments was ₹5,47,880.

Distribute the profit among the partners and prepare partner's current accounts when Capitals are fixed.

SOLUTION :

Books of *A*, *B* and *C*

PROFIT AND LOSS APPROPRIATION ACCOUNT

for the year ended 31st March, 2020

Dr. Cr.

Particulars		₹	Particulars		₹
To Interest on Capital :			By Profit & Loss A/c		
A	25,000		(Net Profit for the year)		5,47,880
B	22,500		By Interest on Drawings :		
C	12,500	60,000	*A* $1,08,000 \times \frac{8}{100} \times \frac{5.5}{12}$	= 3,960	
To Salary :					
A	54,000		*B* $96,000 \times \frac{8}{100} \times \frac{6.5}{12}$	= 4,160	
C	66,000	1,20,000			
To Commission (Note 1)			*C* $50,000 \times \frac{8}{100} \times \frac{6}{12}$	= 2,000	10,120
A	14,000				
C	14,000	28,000			
To Profit transferred to (Note 2)					
A's Current A/c	1,10,000				
B's Current A/c	1,20,000				
C's Current A/c	1,20,000	3,50,000			
		5,58,000			5,58,000

PARTNER'S CURRENT ACCOUNTS

Dr. Cr.

Particulars	*A*	*B*	*C*	Particulars	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Drawings	1,08,000	96,000	50,000	By Int. on Capital	25,000	22,500	12,500
To Int. on Drawings	3,960	4,160	2,000	By Salary	54,000		66,000
To Bal. c/d	91,040	42,340	1,60,500	By Commission	14,000		14,000
				By P & L App. A/c	1,10,000	1,20,000	1,20,000
	2,03,000	1,42,500	2,12,500		2,03,000	1,42,500	2,12,500

Working Notes : (1)

Balance of Profit : ₹5,47,880 + 10,120 – 60,000 – 1,20,000 = ₹3,78,000

Commission to *A* and *C* is 4% to each partner after charging such commission.

Hence, the commission will be $\frac{4}{108}$ to each partner.

Commission to A = $3,78,000 \times \frac{4}{108}$ = ₹14,000

Commission to C = $3,78,000 \times \frac{4}{108}$ = ₹14,000

(2) Divisible Profit = ₹3,78,000 – 14,000 – 14,000 = ₹3,50,000

	A	B	C
	₹	₹	₹
Upto ₹3,00,000 Equally	1,00,000	1,00,000	1,00,000
3,50,000 – 3,00,000 = ₹50,000 in $\frac{1}{5} : \frac{2}{5} : \frac{2}{5}$	10,000	20,000	20,000
	1,10,000	1,20,000	1,20,000

ILLUSTRATION 25.

A and *B* share profits in the ratio of 3 : 2. Their drawings for the year ending 31st March, 2022 were as under :

A	₹	B	₹
1st May, 2021	6,000	1st April, 2021	5,000
30th November, 2021	8,000	31st August, 2021	6,000
31st January, 2022	7,000	31st October, 2021	4,000
		1st February, 2022	2,000
		31st March, 2022	3,000

Calculate interest on drawings @ 15% p.a. for the year ended on 31st March, 2022.

SOLUTION :

A				B			
Date	*Amount*	*Period*	*Products*	*Date*	*Amount*	*Period*	*Products*
2021	₹	Months	₹	2021	₹	Months	₹
1st May	6,000	11	66,000	1st April	5,000	12	60,000
30th November	8,000	4	32,000	31st August	6,000	7	42,000
2022				31st October	4,000	5	20,000
31st January	7,000	2	14,000	2022			
				1st February	2,000	2	4,000
				31st March	3,000	0	0
		Total	1,12,000			Total	1,26,000

Interest on Drawings = $\frac{\text{Total of Products}}{12} \times \frac{\text{Rate of Interest}}{100}$

$A = \frac{1,12,000}{12} \times \frac{15}{100}$ = ₹1,400 ; $B = \frac{1,26,000}{12} \times \frac{15}{100}$ = ₹1,575

Distinction between drawings against profits and drawings against capital :

Basis of Distinction	*Drawings against Profits*	*Drawings against Capital*
1. Part	It is a part of expected profit.	It is a part of capital (*i.e.*, capital withdrawn).

2. Where Debited	It is debited to Drawings Account.	It is debited to Capital Account.
3. Effect on Capital	It does not reduce capital.	It reduces capital.
4. Interest on Drawings	It is considered while calculating interest on drawings.	It is not considered while calculating interest on drawings.
5. Interest on Capital	It is not considered while calculating interest on capital.	It is considered while calculating interest on capital.

Interest is not allowed on Drawings against Capital

Drawing by a partner against capital is debited to his Capital Account. As a result, partner gets interest on the actual capital invested by him into the business. For example, Partner Suresh has capital of ₹10,00,000 on 1st April, 2018 against which he withdraws ₹2,00,000 on 1st July, 2018. Partnership Deed provides interest on capital @ 10% p.a. Interest on capital for the year ended 31st March 2019 will be as follows :

	₹
On ₹10,00,000 @ 10% p.a. for 3 months	25,000
On ₹ 8,00,000 @ 10% p.a. for 9 months	60,000
	85,000

Thus, interest is not allowed on drawings against capital.

Interest is neither allowed nor charged on drawings against capital.

ILLUSTRATION 26.

A, *B* and *C* are in partnership sharing residual profits and losses in the ratio of 5 : 2 : 3 respectively. On 1st April, 2021 their Capital and Current Account balances were :

Partners	*Capital Accounts* ₹	*Current Accounts* ₹
A	16,000	1,160 (Cr.)
B	20,000	700 (Dr.)
C	24,000	420 (Cr.)

By agreement, partners are entitled to interest on capital @ 5% p.a. On 1st October, 2021 by mutual agreement, *A* increased his capital by paying a further ₹4,000 into the partnership bank account, while *B* reduced his capital to ₹12,000, but left his withdrawn capital in the partnership as a loan bearing interest @ 5% p.a.

Partners are allowed to withdraw from current accounts at any time during the financial year but are charged interest on the amount involved. Details of drawings made and interest chargeable in respect of each partner for the financial year ended 31st March, 2022 are :

Partners	*Drawings* ₹	*Interest on Drawings* ₹
A	4,800	180
B	3,600	60
C	6,000	50

B is remunerated for his participation in the running of the partnership by an annual salary of ₹5,000.

The trading profit (before interest) for the year ended 31st March, 2022 was ₹39,810.

You are required to prepare Profit and Loss Appropriation Account and Partners' Capital Accounts, Current Accounts and *B*'s Loan Account.

SOLUTION :

PROFIT AND LOSS APPROPRIATION ACCOUNT
for the year ended 31st March, 2022

Dr. Cr.

Particulars		₹	*Particulars*		₹
To Salary : *B*		5,000	By Profit & Loss A/c (Net Profit)	39,810	
To Interest on Capital A/c :			*Less* : Interest on Loan	200	39,610
A	900		By Interest on Drawings A/c :		
B	800		*A*	180	
C	1,200	2,900	*B*	60	
To Share of Profit transferred to :			*C*	50	290
A's Current A/c (5/10)	16,000				
B's Current A/c (2/10)	6,400				
C's Current A/c (3/10)	9,600	32,000			
		39,900			39,900

PARTNERS' CAPITAL ACCOUNTS

Dr. Cr.

Date	*Particulars*	*A*	*B*	*C*	*Date*	*Particulars*	*A*	*B*	*C*
2021		₹	₹	₹	2021		₹	₹	₹
Oct. 1	To *B*'s Loan A/c	—	8,000	—	Apr. 1	By Bal. b/d	16,000	20,000	24,000
					Oct. 1	By Bank A/c	4,000	—	—
2022									
Mar.31	To Bal. c/d	20,000	12,000	24,000					
		20,000	20,000	24,000			20,000	20,000	24,000

PARTNERS' CURRENT ACCOUNTS

Dr. Cr.

Date	*Particulars*	*A*	*B*	*C*	*Date*	*Particulars*	*A*	*B*	*C*
2021		₹	₹	₹	2021		₹	₹	₹
Apr. 1	To Bal. b/d	—	700	—	Apr. 1	By Bal. b/d	1,160	—	420
2022					2022				
Mar.31	To Drawings A/c	4,800	3,600	6,000	Mar.31	By Salaries A/c	—	5,000	—
Mar.31	To Interest on Drawings A/c	180	60	50	Mar.31	By Interest on Capital A/c	900	800	1,200
Mar.31	To Bal. c/d	13,080	7,840	5,170	Mar.31	By P & L App. A/c (Profit)	16,000	6,400	9,600
		18,060	12,200	11,220			18,060	12,200	11,220

Dr. *B*'s LOAN ACCOUNT Cr.

Date	Particulars	₹	Date	Particulars	₹
2022 March 31	To Balance c/d	8,200	2021 October 1	By *B*'s Capital A/c	8,000
			2022 March 31	By Interest on *B*'s Loan A/c	200
		8,200			8,200

Notes : 1. Interest on Capital :

		₹
A	On ₹16,000 for 6 months	400
	On ₹20,000 for 6 months	500
		900
B	On ₹20,000 for 6 months	500
	On ₹12,000 for 6 months	300
		800
C	On ₹24,000 for One year	1,200

2. Interest on *B*'s Loan : On ₹8,000 for 6 months @ 5% = ₹200

ILLUSTRATION 27.

Anita and Tony, each doing business as sole proprietors, started a partnership on 1st April, 2018. Anita brought in Plant and Machinery valued at ₹5,00,000 whereas Tony brought in furniture costing ₹50,000 and ₹7,00,000 in cash.

Since the business needed more funds, Tony gave a loan of ₹2,00,000 to the firm on 30th June, 2018.

Their partnership deed provided for :

(*a*) Interest on capital to be allowed @ 10% per annum.

(*b*) Interest on drawings to be charged @ 6% per annum.

(*c*) Anita to be given a commission of 4% on the *corrected* net profits before charging commission.

(*d*) Tony to be given a salary of ₹12,000 per annum.

Tony withdrew ₹5,000 at the end of every month and Anita withdrew ₹30,000 on 1st August, 2018.

The net profit of the firm, for the year 2018-19, *after* debiting Tony's salary of ₹12,000 per annum but *before* considering any interest due to and due from the partners, was ₹4,00,000.

You are required to prepare for the year 2018-19 :

(*i*) Profit and Loss Appropriation Account.

(*ii*) Partners' Capital Accounts. *(I.S.C. 2020)*

SOLUTION : PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2019* Cr.

Particulars	₹	Particulars	₹
To Interest on Capital A/c		By Profit & Loss A/c 4,00,000	

Anita	50,000		*Add* : Tony's Salary	12,000	
Tony	75,000	1,25,000	*Less* : Interest on		
To Salary A/c :			Tony's Loan	(9,000)	4,03,000
Tony's Capital A/c		12,000	By Interest on Drawings A/c :		
To Commission :			Anita	1,200	
Anita's Capital A/c (4% of ₹4,03,000)		16,120	Tony	1,650	2,850
To Profits transferred to :					
Anita's Capital A/c		1,26,365			
Tony's Capital A/c		1,26,365			
		4,05,850			4,05,850

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*Anita*	*Tony*	*Particulars*	*Anita*	*Tony*
	₹	₹		₹	₹
To Drawings	30,000	60,000	By Plant & Machinery	5,00,000	—
To Interest on Drawings	1,200	1,650	By Furniture	—	50,000
To Balance c/d	6,61,285	9,01,715	By Bank		7,00,000
			By Interest on Capital	50,000	75,000
			By Salary		12,000
			By Commission	16,120	
			By P&L App. A/c	1,26,365	1,26,365
	6,92,485	9,63,365		6,92,485	9,63,365

Working Notes :

1. **Capitals :**

		₹
Anita :	Plant & Machinery	5,00,000
Tony :	Furniture	50,000
	Bank	7,00,000
		7,50,000

2. **Interest on Capitals :**

Anita :	10% on ₹5,00,000	50,000
Tony :	10% on ₹7,50,000	75,000

3. **Interest on Drawings :**

Anita :	6% on ₹30,000 for 8 months	1,200
Tony :	$60{,}000 \times \frac{6}{100} \times \frac{5.5}{12}$	1,650

4. **Interest on Tony's Loan :**

$$2{,}00{,}000 \times \frac{6}{100} \times \frac{9}{12} = ₹9{,}000$$

ILLUSTRATION 28.

X, *Y* and *Z* are in partnership with capitals of ₹1,20,000 (Credit); ₹1,00,000 (Credit) and ₹8,000 (Debit) respectively on 1st April, 2021 :

Their partnership deed provides the following :

(*i*) Partners are to be allowed interest on capitals @ 5% p.a. and are to be charged interest on drawings @ 6% p.a.

(*ii*) X is entitled to a commission of 10% of the net profit before charging such commission.

(*iii*) Y is also entitled to a commission of 10% of the net profit after charging his commission and clause (*ii*) above.

(*iv*) Z is entitled to a rent of ₹1,000 per month for the use of his premises by the firm.

During the year, X withdrew ₹200 at the beginning of every month, Y ₹300 during the month and Z ₹400 at the end of every month.

The net profit of the firm for the year ended 31st March, 2022 before providing for any of the above clauses was ₹1,11,000.

From the above you are required to draft only the Profit and Loss Appropriation Account for the year ended 31st March, 2022.

SOLUTION :

Books of X, Y and Z

PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *For the year ending 31st March, 2022* Cr.

Particulars		₹	*Particulars*	₹
To Interest on Capitals :			By Profit & Loss A/c (Net Profit for the year) (See Note 1)	99,000
X	6,000			
Y	5,000	11,000	By Interest on Drawings :	
To Commission :				
X: 10% on 99,000	9,900		X: ₹ $2{,}400 \times \frac{6}{100} \times \frac{6.5}{12} = 78$	
Y: 10/110 on (99,000 – 9,900)	8,100	18,000	Y: ₹ $3{,}600 \times \frac{6}{100} \times \frac{6}{12} = 108$	
To Share of Profit :				
X's Capital A/c	23,439		Z: ₹ $4{,}800 \times \frac{6}{100} \times \frac{5.5}{12} = 132$	318
Y's Capital A/c	23,439			
Z's Capital A/c	23,440	70,318		
		99,318		99,318

Note : (1) Rent payable to a partner for use of his premises is an item of Profit and Loss Account since it is a charge against profits and not an appropriation of profits. It is an item to be debited to P & L A/c. Hence the profits will have to be adjusted for the rent, *i.e.*,

		₹
Net Profit before any adjustment	=	1,11,000
Less : Rent @ ₹1,000 per month	=	12,000
		99,000

ILLUSTRATION 29.

A, B and C are partners sharing profit and loss in the ratio of 3 : 2 : 1. A withdraws ₹2,000 at the beginning of every month, B withdraws ₹1,500 in the middle of every month whereas C withdraws ₹1,000 at the end of every month. Interest on capitals and drawings is to be charged @10% p.a. C is also to be allowed a salary of ₹800 per month. After deducting salary but before allowing any type of interest, the profit for the year ending 31st March, 2022 was ₹1,22,150. Prepare Profit and Loss Appropriation Account, Partner's Capital Accounts and Current Accounts from the additional information given below :—

	A (₹)	B (₹)	C (₹)
Capital Accounts on 1st April, 2021	2,00,000	1,50,000	1,00,000
Additional Capitals introduced on 1st July, 2021	50,000	30,000	—
Capital withdrawn on 1st January, 2022	—	—	20,000
Current Accounts on 1st April, 2021	12,200	5,500	4,100 (Dr.)
Loan Account on 1st April, 2021	40,000	—	—

SOLUTION : PROFIT AND LOSS APPROPRIATION ACCOUNT

for the year ended 31st March, 2022

Dr. Cr.

Particulars		₹	Particulars		₹
To Interest on Capital :			By Profit & Loss A/c		
A	23,750		(Net Profit)	1,22,150	
B	17,250		*Less* : Interest on		
C	9,500	50,500	*A*'s Loan @ 6%		
To Profits transferred to			p.a. on ₹40,000	2,400	1,19,750
A's Current A/c 3/6	36,000		By Interest on Drawings :		
B's Current A/c 2/6	24,000		*A*	1,300	
C's Current A/c 1/6	12,000	72,000	*B*	900	
			C	550	2,750
		1,22,500			1,22,500

Dr. CAPITAL ACCOUNTS Cr.

Particulars	A	B	C	Particulars	A	B	C
	₹	₹	₹		₹	₹	₹
To Bank	—	—	20,000	By Bal. b/d	2,00,000	1,50,000	1,00,000
To Bal. c/d	2,50,000	1,80,000	80,000	By Bank	50,000	30,000	—
	2,50,000	1,80,000	1,00,000		2,50,000	1,80,000	1,00,000

Dr. CURRENT ACCOUNTS Cr.

Particulars	A	B	C	Particulars	A	B	C
	₹	₹	₹		₹	₹	₹
To Bal. b/d	—	—	4,100	By Bal. b/d	12,200	5,500	—
To Drawings	24,000	18,000	12,000	By Interest on Capitals	23,750	17,250	9,500
To Int. on Drawings	1,300	900	550	By Salary			9,600
To Bal. c/d	46,650	27,850	14,450	By P&L. App. A/c (Profit)	36,000	24,000	12,000
	71,950	46,750	31,100		71,950	46,750	31,100

Working Notes :—

(1) Calculation of Interest on Drawings :—

Interest on *A*'s Drawings will be calculated for $6\frac{1}{2}$ months :—

$$24{,}000 \times \frac{10}{100} \times \frac{6.5}{12} = ₹1{,}300$$

Interest on *B*'s Drawings will be calculated for 6 months :—

$$18{,}000 \times \frac{10}{100} \times \frac{6}{12} = ₹900$$

Interest on *C*'s Drawings will be calculated for $5\frac{1}{2}$ months :—

$$12{,}000 \times \frac{10}{100} \times \frac{5.5}{12} = ₹550$$

(2) Calculation of Interest on Capitals :—

		₹
On *A*'s Capital :	On ₹2,00,000 from 1st April to 30th June (3 months)	5,000
	On ₹2,50,000 from 1st July to 31st March (9 months)	18,750
		23,750
On *B*'s Capital :	On ₹1,50,000 from 1st April to 30th June (3 months)	3,750
	On ₹1,80,000 from 1st July to 31st March (9 months)	13,500
		17,250
On *C*'s Capital :	On ₹1,00,000 from 1st April to 31st December (9 months)	7,500
	On ₹ 80,000 from 1st Jan. to 31st March (3 months)	2,000
		9,500

(3) Rate of interest on Partner's Loan is not given in the question. Hence, under the Partnership Act 6% p.a. interest will be allowed on Loan.

(4) Interest on Loan is not recorded in the Current Account.

ILLUSTRATION 30.

Tej, Partho and Ginni are in partnership sharing profits and losses in the ratio of 2 : 1 : 1. Throughout the half year ended 31st March, 2017 their capital accounts have remained unchanged at ₹60,000, ₹40,000 and ₹30,000 respectively.

Their current account balances on 1st October, 2016 were :

Tej	₹ 8,500 (Dr.)
Partho	₹ 6,000 (Dr.)
Ginni	₹10,000 (Cr.)

During the six month period in 2016-17, Tej withdrew ₹200 at the beginning of each month, Partho withdrew ₹400 at the end of each month while Ginni withdrew ₹1,800 during the period of six months.

Their partnership deed provides that :

(*a*) Partners are allowed interest on capital @ 5% p.a.

(*b*) Partners are allowed or charged interest on current account balances @ 4% p.a.

(*c*) Interest on drawings to be charged @ 6% p.a.

(*d*) Partho to be is entitled to a salary of ₹500 per month.

(*e*) Tej to be entitled to a commission of 5% of the correct net profit of the firm after charging such commission.

During the half year ended 31st March, 2017, the net profit of the firm was ₹2,07,000 after charging Partho's salary which had been debited to wages and salaries account.

You are required to prepare the profit and loss appropriation account of the firm for the half year ending 31st March, 2017. *(ISC Sample Paper 2018)*

SOLUTION: PROFIT & LOSS APPROPRIATION ACCOUNT

for the half year ended 31st March, 2017

Dr. Cr.

Particulars		₹	*Particulars*		₹
To Interest on Capital :			By Profit & Loss A/c		
Tej	1,500		(Net profit for the period)		
Partho	1,000		(₹2,07,000 + ₹3,000)		2,10,000
Ginni	750	3,250	By Interest on Current A/c :		
To Interest on Current A/c :			Tej	170	
Ginni		200	Partho	120	290
To Salary : Partho		3,000	By Interest on Drawings :		
To Commission :			Tej	21	
Tej (2,10,000 × $\frac{5}{105}$)		10,000	Partho	30	
			Ginni	27	78[1]
To Profit transferred to :					
Tej's Current A/c 2/4	96,959				
Partho's Current A/c 1/4	48,480				
Ginni's Current A/c 1/4	48,479	1,93,918			
		2,10,368			2,10,368

Working Notes :

(1) Calculation of interest on drawings :

Tej $1{,}200 \times \frac{6}{100} \times \frac{3.5}{12} = ₹21$

Partho $2{,}400 \times \frac{6}{100} \times \frac{2.5}{12} = ₹30$

Ginni $1{,}800 \times \frac{6}{100} \times \frac{3}{12} = ₹27$

When a fixed amount is withdrawn at the beginning of every month during 6 months, interest will be charged for 3.5 months. In case of drawings at the end of every month, interest will be charged for 2.5 months.

ILLUSTRATION 31.

Sanjay, Madhav and Bijoy are partners in a registered firm. Balances of their Capital accounts as on 1st April, 2021 were ₹25,000, ₹15,000 and ₹5,000 respectively. The partnership agreement provides :

(*i*) Bijoy shall be credited with a salary of ₹300 per month.

(*ii*) Interest on Capital is allowed @ 10% per annum and interest on drawings is charged @ 15% per annum.

(*iii*) After providing (*i*) and (*ii*) mentioned above and after making a provision for extra remuneration mentioned in this para (*iii*). Bijoy shall be entitled to 5% of all the profits in excess of ₹7,000.

(*iv*) Madhav is to have one-fifth of the profit after charging all amounts under (*i*) to (*iii*) above and in this para (*iv*). The balance of profits is to be divided between Sanjay and Bijoy in the ratio of 7 : 1 respectively.

Bijoy contributed additional capital of ₹5,000 on 1st October, 2021. Sanjay has withdrawn ₹2,000 on 1st August, 2021 and ₹1,600 on 31st December, 2021, whereas Bijoy did not withdraw any amount. Madhav has withdrawn ₹400 at the end of each quarter.

The net profit for the year ended 31st March, 2022 before making above adjustments was ₹40,500.

You are required to prepare profit and loss appropriation account for the year ended 31st March, 2022 and the partners' capital accounts.

SOLUTION : PROFIT & LOSS APPROPRIATION ACCOUNT

for the year ended 31st March, 2022

Dr. Cr.

Particulars		₹	Particulars		₹
To Interest on capital :			By Profit & Loss A/c		
Sanjay	2,500		(Net Profit)		40,500
Madhav	1,500		By Interest on Drawings :		
Bijoy	750	4,750	Sanjay	260	
To Salary to Bijoy			Madhav	90	350
12 × ₹300	3,600				
Extra remuneration	1,214	4,814			
To Profit transferred to :					
Madhav's Capital A/c 20/120 or 1/6 × ₹31,286	5,214				
Sanjay's Capital A/c 7/8 × ₹(31,286 –5,214)	22,813				
Bijoy's Capital A/c 1/8 × ₹(31,286–5,214)	3,259	31,286			
		40,850			40,850

CAPITAL ACCOUNTS

Dr. Cr.

Particulars	Sanjay	Madhav	Bijoy	Particulars	Sanjay	Madhav	Bijoy
31.3.2022	₹	₹	₹	1.4.2021	₹	₹	₹
To Drawings	3,600	1,600	—	By Balance b/d	25,000	15,000	5,000
To Interest on Drawings	260	90	—	1.10.2021 By Bank	—	—	5,000
To Balance c/d	46,453	20,024	18,823	31.3.2022 By Interest on Capital	2,500	1,500	750
				By Salary	—	—	4,814

				By Share of Profit	22,813	5,214	3,259
	50,313	21,714	18,823		50,313	21,714	18,823
				1.4.2022 By Balance b/d	46,453	20,024	18,823

Working Notes :

(*i*) Interest on Capitals (@ 10% p.a.)

			₹
Sanjay :	on ₹25,000 for full year		2,500
Madhav :	on ₹15,000 for full year		1,500
Bijoy :	on ₹ 5,000 for full year	500	
	on ₹ 5,000 for 6 months	250	750

(*ii*) Interest on Drawings (@ 15% p.a.)

(*a*) Sanjay :

Date	*Amount* ₹	*Period*	*Products* ₹
Aug. 1, 2021	2,000	8 months	16,000
Dec. 31, 2021	1,600	3 months	4,800
			20,800

Interest = $₹20,800 \times \frac{15}{100} \times \frac{1}{12} = ₹260$

(*b*) Madhav :

Date	*Amount* ₹	*Period*	*Products* ₹
June 30, 2021	400	9 months	3,600
Sept. 30, 2021	400	6 months	2,400
Dec. 31, 2021	400	3 months	1,200
March 31, 2022	400	Nil	—
			7,200

Interest = $₹7,200 \times \frac{15}{100} \times \frac{1}{12} = ₹90$

(*iii*) Calculation of extra remuneration to Bijoy :

Profit after interest on drawings, interest on capital and salary :

= ₹(40,500 + 350 – 4,750 – 3,600) = ₹32,500

Amount on which extra remuneration is to be provided :

= ₹32,500 – ₹7,000 = ₹25,500

Extra Remuneration = $\frac{5}{105} \times 25,500 = ₹1,214.$

Interest on Capital

Provisions relating to Interest on capital are given below :—

Case	*Provision*
Case I : When the partnership agreement is silent about the interest on Capital.	No interest will be allowed on Capital.

Case II :	When the partnership agreement provides for interest on capital but is silent in treating interest as a charge[1] or appropriation.[2]	Interest on capital will be allowed only when there is a profit.	
		(a) In case of loss :	No interest will be allowed on capital.
		(b) When the profit before interest is equal to or more than the amount of interest.	Full interest will be allowed.
		(c) When the profit before interest is less than the interest itself.	Interest will be restricted to the amount of profit. Hence, profit will be distributed in the ratio of interest on capital of each partner.
Case III:	When the partnership agreement provides for treating interest as a charge.	Full interest will be allowed whether there is profit or loss.	

(1) **Charge :**— Charge means full interest is to be allowed whether there are profits or losses.

(2) **Appropriation :**— Appropriation means interest is to be allowed only out of profits. It means that the interest on capital cannot exceed the amount of profit.

ILLUSTRATION 32.

A and *B* are partners sharing the profits and losses in the ratio of 3 : 2 with capitals of ₹2,00,000 and ₹1,00,000 respectively. Show the distribution of profits in each of the following alternative cases :

Case (*i*) If the partnership deed is silent as to the Interest on Capital and the profits for the year are ₹50,000.

Case (*ii*) If the partnership deed provides for Interest on Capital @ 8% p.a. and the losses for the year are ₹50,000.

Case (*iii*) If the partnership deed provides for Interest on Capital @ 8% p.a. and the profits for the year are ₹50,000.

Case (*iv*) If the partnership deed provides for Interest on Capital @ 8% p.a. and the profits for the year are ₹15,000.

Case (*v*) If the partnership deed provides for Interest on Capital @ 8% p.a. even if it involves the firm in loss and the profits for the year are ₹15,000.

SOLUTION :

Case (*i*)

Dr. PROFIT AND LOSS APPROPRIATION A/C Cr.

Particulars		₹	*Particulars*	₹
To Profit transferred to :			By Profit & Loss A/c (Profit for the year)	50,000
A's Capital A/c 3/5	30,000			
B's Capital A/c 2/5	20,000	50,000		
		50,000		50,000

Note : If the partnership deed is silent, no interest will be allowed on capitals.

Case (*ii*)

Dr. PROFIT AND LOSS A/C Cr.

Particulars		₹	*Particulars*		₹
To Balance b/d			By Loss transferred to :		
(Loss for the year)		50,000	*A*'s Capital A/c 3/5	30,000	
			B's Capital A/c 2/5	20,000	50,000
		50,000			50,000

Note : (*i*) Interest on Capital will not be provided in case of loss.
(*ii*) Profit & Loss Appropriation A/c will not be prepared in case of loss.

Case (*iii*)

Dr. PROFIT AND LOSS APPROPRIATION A/C Cr.

Particulars		₹	*Particulars*	₹
To Interest on Capital :			By Profit & Loss A/c	
A	16,000		(Profit for the year)	50,000
B	8,000	24,000		
To Profit transferred to :				
A's Capital A/c 3/5	15,600			
B's Capital A/c 2/5	10,400	26,000		
		50,000		50,000

Case (*iv*)

Dr. PROFIT AND LOSS APPROPRIATION A/C Cr.

Particulars	₹	*Particulars*	₹
To Interest on Capital :		By Profit & Loss A/c	
$A\ 15{,}000 \times \frac{2}{3}$	10,000	(Profit for the year)	15,000
$B\ 15{,}000 \times \frac{1}{3}$	5,000		
	15,000		15,000

Note : The available profit is ₹15,000 whereas the interest due on capitals is ₹24,000 (*i.e.* ₹16,000 + ₹8,000). Since the profit is less than the interest, the available profit will be distributed in the ratio of interest *i.e.*, 16,000 : 8,000 or 2 : 1.

Case (*v*)

Dr. PROFIT AND LOSS A/C Cr.

Particulars		₹	*Particulars*		₹
To Interest on Capital :*			By Balance b/d		
A	16,000		(Profit for the year)		15,000
B	8,000	24,000	By Loss transferred to :		
			A's Capital A/c 3/5	5,400	
			B's Capital A/c 2/5	3,600	9,000
		24,000			24,000

* Interest on capital will be allowed even if firm incurs loss. It means interest on capital is a charge against profit. As such, it would be debited to profit and loss and not to profit and loss appropriation account.

ILLUSTRATION 33.

(Calculation of Interest on capital when the profits are inadequate)

A and *B* contribute ₹5,00,000 and ₹3,00,000 respectively by way of capital on which they agree to allow interest at 6% p.a. Their respective share of profit is 3 : 2 and the profit for the year is ₹40,000 before allowing interest on capitals. Prepare the necessary account to allocate interest on capitals in the following cases :

(*i*) When the Partnership Deed is silent about the treatment of interest on Capital, and

(*ii*) When interest is a charge as per Partnership Deed.

SOLUTION :

(I) When partnership deed is silent in treating interest as a charge or appropriation: In such a case interest will be allowed upto the extent of available profit.

Dr. PROFIT AND LOSS APPROPRIATION A/C Cr.

Particulars	₹	*Particulars*	₹
To Interest on Capital A/c		By Profit & Loss A/c	
A 40,000 × $\frac{5}{8}$	25,000	(Profit for the year)	40,000
B 40,000 × $\frac{3}{8}$	15,000		
	40,000		40,000

Working Note :

		₹
Interest on *A*'s Capital		30,000
Interest on *B*'s Capital		18,000
	Total Interest	48,000

The available profit is ₹40,000 whereas the interest due on capitals is ₹48,000. Since the profit is less than interest, the available profit will be distributed in the ratio of interest *i.e.*, 30,000 : 18,000 or 5 : 3.

(II) When interest is a charge as per Partnership Deed : In such a case interest will be allowed irrespective of profit :—

Dr. PROFIT AND LOSS A/C Cr.

Particulars	₹	*Particulars*		₹
To Interest on Capital A/c		By Balance b/d		40,000
A	30,000	(Profit for the year)		
B	18,000	By Loss Transferred to :		
		A's Capital A/c	4,800	
		B's Capital A/c	3,200	8,000
	48,000			48,000

ILLUSTRATION 34.

E, F and *G* were partners in a firm sharing profits in the ratio of 3 : 3 : 4. Their respective fixed capitals were *E* ₹3,00,000; *F* ₹4,00,000 and *G* ₹5,00,000. The partnership deed provided for allowing interest on capital @ 12% p.a. even if it results into a loss to the firm. The net profit of the firm for the year ended 31st March, 2018 was ₹1,10,000.

Pass necessary journal entries for allowing interest on capital and division of profit/loss in the books of the firm. *(C.B.S.E. 2019, Kerala)*

SOLUTION :

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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2018	Interest on Capital A/c	Dr.		1,44,000	
March 31	To *E*'s Current A/c				36,000
	To *F*'s Current A/c				48,000
	To *G*'s Current A/c				60,000
	(Interest on Capital Credited to Partner's Current A/cs)				
,,	Profit & Loss A/c	Dr.		1,44,000	
	To Interest on Capital A/c				1,44,000
	(Interest on Capital debited to Profit & Loss A/c)				
,,	*E*'s Current A/c	Dr.		10,200	
	F's Current A/c	Dr.		10,200	
	G's Current A/c	Dr.		13,600	
	To Profit & Loss A/c				34,000
	(Net loss transferred to Current Accounts)				

ILLUSTRATION 35.

A and *B* entered into partnership with capitals of ₹4,00,000 and ₹2,00,000 respectively and agreed to share profits & losses in the ratio of 3 : 2. Their partnership deed provided that interest on capital shall be allowed at 6% p.a. and it is to be treated as a charge against profits. Prepare the relevant account to allocate the profit in the following alternative cases :

(*i*) If profit for the year is ₹80,000;

(*ii*) If profit for the year is ₹20,000;

(*iii*) If loss for the year is ₹20,000.

SOLUTION :

Case (*i*)

Dr. PROFIT AND LOSS ACCOUNT Cr.

Particulars		₹	Particulars	₹
To Interest on Capital :			By Balance b/d	
A	24,000		(Profit before interest)	80,000
B	12,000	36,000		

To Profit transferred to Profit & Loss Appropriation A/c	44,000		
	80,000		80,000

Dr. PROFIT AND LOSS APPROPRIATION ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Profit transferred to :		By Profit & Loss A/c	44,000
A's Capital A/c (3/5) 26,400			
B's Capital A/c (2/5) 17,600	44,000		
	44,000		44,000

Note : Since interest on capital is a charge against profit, it will be debited to Profit & Loss A/c and not to Profit & Loss Appropriation A/c.

Case (*ii*)

Dr. PROFIT AND LOSS ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Interest on Capital :		By Balance b/d	
A 24,000		(Profit before interest)	20,000
B 12,000	36,000	By Loss transferred to :	
		A's Capital A/c (3/5) 9,600	
		B's Capital A/c (2/5) 6,400	16,000
	36,000		36,000

Case (*iii*)

Dr. PROFIT AND LOSS ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance b/d (Loss for the year)	20,000	By Loss transferred to :	
To Interest on Capital :		*A*'s Capital A/c (3/5) 33,600	
A 24,000		*B*'s Capital A/c (2/5) 22,400	56,000
B 12,000	36,000		
	56,000		56,000

ILLUSTRATION 36.

Shikha and Fatima were partners in a firm sharing profits in the ratio of 5 : 3. Their fixed capitals on 1.4.2021 were : Shikha ₹3,00,000 and Fatima ₹4,00,000. They agreed to allow interest on capital @ 12% per annum and to charge on drawings @15% per annum. The profit of the firm for the year ended 31.3.2022 before all above adjustments were ₹63,000. The drawings made by Shikha were ₹10,000 and by Fatima ₹20,000 during the year. Prepare Profit and Loss Appropriation Account. The interest on capital will be allowed even if the firm incurs a loss.

SOLUTION : **In the Books of Shikha and Fatima**

PROFIT AND LOSS A/C

for the year ended 31st March, 2022

Dr. Particulars	₹	Particulars	Cr. ₹
To Interest on Capital*		By Balance b/d	
Shikha's Current A/c 36,000		(Profit before interest)	63,000
Fatima's Current A/c 48,000	84,000	By Profit and Loss Appropriation A/c (loss transferred)	21,000
	84,000		84,000

PROFIT AND LOSS APPROPRIATION A/C

for the year ended 31st March, 2022

Dr. Particulars	₹	Particulars	Cr. ₹
To Profit and Loss A/c		By Interest on Drawings :	
(loss transferred)	21,000	Shikha's Current A/c 750	
		Fatima's Current A/c 1,500	2,250
		By Net Loss transferred to :	
		Shikha's Current A/c 11,719	
		Fatima's Current A/c 7,031	18,750
	21,000		21,000

Note : As the time period of drawings is not given, the interest on drawings will be charged for 6 months :

$$\text{Shikha} = ₹10{,}000 \times \frac{15}{100} \times \frac{6}{12} = ₹\ 750$$

$$\text{Fatima} = ₹20{,}000 \times \frac{15}{100} \times \frac{6}{12} = ₹1{,}500$$

* In this question, Interest on capital is to be allowed even if firm incurs loss. It means interest on capital is a charge against profit. As such, it should be debited to profit and loss and not to profit and loss appropriation account.

ILLUSTRATION 37.
(Appropriation of Profit according to Capital Ratio)

A, *B* and *C* started a business in partnership. *A* contributes ₹50,000 for the whole year. *B* introduces ₹40,000 at first and increased it to ₹46,000 at the end of four months but withdraws ₹16,000 at the end of nine months. *C* invests ₹80,000 at first but withdraws ₹20,000 at the end of five months.

Firm earned a profit of ₹23,750 during the year. You are required to show the division of profits on the basis of the effective capital employed by each partner during the year.

SOLUTION :

Ratio of effective capital will be calculated as under :—

	Products
A : ₹50,000 for the whole 12 months	6,00,000

B :	₹40,000 for 4 months	1,60,000
	₹46,000 for 5 months	2,30,000
	₹30,000 for 3 months	90,000
		4,80,000
C :	₹80,000 for 5 months	4,00,000
	₹60,000 for 7 months	4,20,000
		8,20,000

Thus the profit sharing ratio would be : 6,00,000 : 4,80,000 : 8,20,000 or 30 : 24 : 41

Dr. PROFIT AND LOSS APPROPRIATION ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Profits transferred to :		By Profit & Loss A/c	
A's Capital A/c ₹23,750 × $\frac{30}{95}$	7,500	(Net Profit during the year)	23,750
B's Capital A/c ₹23,750 × $\frac{24}{95}$	6,000		
C's Capital A/c ₹23,750 × $\frac{41}{95}$	10,250		
	23,750		23,750

ILLUSTRATION 38.
(Calculation of Capital Ratio)

A and *B* started business on 1st April, 2021 with capitals of ₹60,000 and ₹40,000 respectively. They decided to share profits in the capital ratio. On the basis of the following details, you are required to calculate capital ratio on 31st March, 2022 and interest on capital if it is @ 8% p.a.

	Capital Introduced		Capital Withdrawn	
	A (₹)	B (₹)	A (₹)	B (₹)
1st June, 2021	—	10,000	5,000	—
1st Sept. 2021	15,000	—	—	12,000
1st Oct. 2021	—	20,000	—	—
1st Jan. 2022	—	—	20,000	23,000
1st March, 2022	5,000	—	—	7,000

SOLUTION :

		Products
A :	₹60,000 for 2 months	1,20,000
	₹55,000 for 3 months	1,65,000
	₹70,000 for 4 months	2,80,000
	₹50,000 for 2 months	1,00,000
	₹55,000 for 1 month	55,000
		7,20,000
B :	₹40,000 for 2 months	80,000
	₹50,000 for 3 months	1,50,000

₹38,000 for 1 month	38,000
₹58,000 for 3 months	1,74,000
₹35,000 for 2 months	70,000
₹28,000 for 1 month	28,000
	5,40,000

On the basis of the products of both the partners the Capital Ratio between them is 7,20,000 : 5,40,000 or 4 : 3.

Interest on A's Capital $= 7{,}20{,}000 \times \frac{8}{100} \times \frac{1}{12} =$ ₹4,800

Interest on B's Capital $= 5{,}40{,}000 \times \frac{8}{100} \times \frac{1}{12} =$ ₹3,600

Adjustments Before the Closing of Partnership Accounts

If it is discovered before the closing of the partnership accounts that certain errors have been made in the accounts, such errors can be rectified before the closing of the accounts itself. For example, if an item of expense has not been recorded then the year's net profits will be reduced by that amount.

ILLUSTRATION 39.

A, *B* and *C* are in partnership sharing profits and losses in the ratio of 2 : 1 : 1. Interest on capitals is 5% per annum and interest on drawings is 4% per annum. (No interest is charged/allowed on current accounts). Following are the particulars of the Capital, Current and Drawings Accounts of the partners :

	(A)	(B)	(C)
	₹	₹	₹
Capital (1-4-2021)	75,000	40,000	30,000
Current A/c (1-4-2021)	10,000	5,000	5,000 (Dr.)
Drawings	15,000	10,000	10,000
Interest on Drawings	500	190	350

The accounts for the year ended 31st March, 2022 showed a net profit of ₹60,000 before taking into account interest on capitals and drawings and following rectifications of errors are to be made: (*a*) Rent of the private house of *A* amounting to ₹750 paid by the firm on 31st March, 2022 has been charged to Rent A/c of the firm. (*b*) Repairs of machinery amounting to ₹10,000 has been debited to Machinery Account and depreciation thereon has been charged @ 20%. (*c*) Travelling expenses of ₹3,000 of *B* for a pleasure trip to U.K. paid by the firm on 30th September, 2021 has been debited to Travelling Expenses Account.

Prepare Profit and Loss Appropriation Account for the year ended 31st March, 2022 and the partners' current accounts for the year.

SOLUTION : PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *(For the year ending on 31st March, 2022)* Cr.

Particulars	₹	*Particulars*	₹
To Interest on Capital A/cs :		By Profit & Loss A/c	55,750

A	3,750		(Net Profit[(1)])		
B	2,000		By Interest on Drawings A/cs :		
C	1,500	7,250	*A*	500	
To Profit transferred to :			*B*	250[(2)]	1,100
A's Current A/c	24,800		*C*	350	
B's Current A/c	12,400				
C's Current A/c	12,400	49,600			
		56,850			56,850

			₹	₹
Note :	**(1)** Net Profit			60,000
	Add :	Rent	750	
		Travelling Expenses	3,000	3,750
				63,750
	Less :	Repairs to Plant	10,000	
		(–) Depreciation 20% on 10,000	2,000	8,000
				55,750

Note : (2) Interest on Drawings of *B* : $₹190 + \frac{3,000 \times 4 \times 1}{100 \times 2} = ₹190 + ₹60 = ₹250$

Dr. PARTNERS' CURRENT ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Balance b/d	—	—	5,000	By Balance b/d	10,000	5,000	—
To Drawings A/c	15,000	13,000[(3)]	10,000	By Int. on Capitals	3,750	2,000	1,500
To Rent	750	—	—	By Profit & Loss Appropriation			
To Interest on Drawings	500	250	350	A/c	24,800	12,400	12,400
To Balance c/d	22,300	6,150	—	By Balance c/d	—	—	1,450
	38,550	19,400	15,350		38,550	19,400	15,350

Note : (3) *B*'s Drawings = ₹10,000 + ₹3,000 for travelling expenses.

Past Adjustments
OR
Adjustments in the Closed Accounts

Sometimes, after the accounts of the partnership firm have been closed after the financial year, it is discovered that there have been some errors or omissions in the accounts. Usually the following types of errors and omissions are discovered :

(1) When Interest on Capitals or Drawings may have been omitted.

(2) When Profits and Losses have been distributed among the partners in a wrong proportion.

(3) When profit sharing ratio has been altered with effect from some past date.

(4) When salary or commission payable to a person has been omitted.

In such cases, instead of altering the closed accounts and the signed balance sheet rectification or adjustment is made at the beginning of the next year.

These errors or omissions may be rectified in two ways :

(A) By passing a single adjustment entry with the net effect of the errors and omissions; or

(B) By passing separate adjustment entries for each error and omission.

(A) **When a Single Adjustment Entry is passed** : In this case, a single adjustment entry is passed with the net amount of all the past adjustments :

ILLUSTRATION 40.

A, B, C and *D* are equal partners in a firm. Their capitals on 1st April, 2019 were ₹50,000; ₹30,000; ₹25,000 and ₹15,000 respectively. After closing the accounts for the year ended 31st March, 2020 it was discovered that according to the partnership deed interest @ 10% per annum on partners' Capitals was not provided before distribution of profits. It was agreed among the partners to make the adjusting entry at the beginning of the next year rather than to alter the Balance Sheet. Pass the necessary journal entry assuming that the capitals are not fixed.

SOLUTION :

		₹
Interest on *A*'s Capital of ₹50,000 @ 10%	=	5,000
Interest on *B*'s Capital of ₹30,000 @ 10%	=	3,000
Interest on *C*'s Capital of ₹25,000 @ 10%	=	2,500
Interest on *D*'s Capital of ₹15,000 @ 10%	=	1,500
Total Interest to be allowed		₹ 12,000

This amount of ₹12,000 is an item of expense for the firm but this has not been recorded on the debit side of P & L Appropriation A/c of the previous year. As such the profit of the previous year will be reduced by this amount. Hence, this loss of ₹12,000 will be shared by the partners in their profit sharing ratio. Therefore, each partner should bear $\frac{12,000}{4}$ = ₹3,000 as loss. This loss should be debited to their respective capital accounts and interest on capitals which they are entitled should be Credited to their Capital accounts.

TABLE SHOWING ADJUSTMENT

	A	*B*	*C*	*D*	Total
	₹	₹	₹	₹	₹
Interest on Capital (Cr.)	5,000	3,000	2,500	1,500	12,000
Division of ₹12,000 in profit sharing ratio, *i.e.*, equally (Dr.)	3,000	3,000	3,000	3,000	12,000
Difference	Cr. 2,000	—	Dr. 500	Dr. 1,500	—

Necessary adjustment entry can be passed as follows :

JOURNAL ENTRY

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2020					
April 1	C's Capital A/c	Dr.		500	
	D's Capital A/c	Dr.		1,500	
	To A's Capital A/c				2,000
	(Adjustment in respect of interest on capital omitted in previous year's accounts)				

ILLUSTRATION 41.

The partners of a firm, Alia, Bhanu and Chand distributed the profits for the year ended 31st March, 2017, ₹80,000 in the ratio of 3 : 3 : 2 without providing for the following adjustments :

(a) Alia and Chand were entitled to a salary of ₹1,500 each p.m.

(b) Bhanu was entitled for a salary of ₹4,000 p.a.

Pass the necessary Journal entry for the above adjustments in the books of the firm. Show workings clearly. *(C.B.S.E. Sample Paper, 2020)*

SOLUTION : TABLE SHOWING ADJUSTMENT

		Alia (₹)	Bhanu (₹)	Chand (₹)	Total (₹)
Salary	(Cr.)	18,000	4,000	18,000	40,000
Division of ₹40,000 in 3 : 3 : 2	(Dr.)	15,000	15,000	10,000	40,000
Difference		Cr. 3,000	Dr. 11,000	Cr. 8,000	—

RECTIFYING JOURNAL ENTRY

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2017					
April 1	Bhanu's Capital A/c	Dr.		11,000	
	To Alia's Capital A/c				3,000
	To Chand's Capital A/c				8,000
	(Adjustment for omission of partner's salaries)				

Note : Profit of ₹80,000 given in the question will be ignored. It will be taken into consideration only when it has been distributed in wrong profit sharing ratio.

ILLUSTRATION 42.

A, B and C are partners in a firm. They have omitted interest on capital @ 10% p.a. for three years ended 31st March, 2020. Their fixed capitals on which interest was to be calculated throughout were :

A	₹1,00,000
B	₹ 80,000
C	₹ 70,000

Give the necessary adjusting journal entry with working notes.

SOLUTION :

Calculation of Interest for 3 years :

		₹
A : 10% on ₹1,00,000 for 3 years	=	30,000
B : 10% on ₹ 80,000 for 3 years	=	24,000
C : 10% on ₹ 70,000 for 3 years	=	21,000
		75,000

TABLE SHOWING ADJUSTMENT

		A	*B*	*C*	Total
		₹	₹	₹	₹
Interest on Capital	(Cr.)	30,000	24,000	21,000	75,000
Division of ₹75,000 in profit sharing ratio, *i.e.*, equally	(Dr.)	25,000	25,000	25,000	75,000
Difference		Cr. 5,000	Dr. 1,000	Dr. 4,000	—

JOURNAL ENTRY

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2020 April 1	*B*'s Current A/c	Dr.		1,000	
	C's Current A/c	Dr.		4,000	
	To *A*'s Current A/c				5,000
	(Omission of interest on capital for three years rectified)				

Note : Since the capitals are fixed, Current Accounts will be debited or credited.

ILLUSTRATION 43.

X, *Y* and *Z* are partners sharing profits and losses in the ratio of 3 : 2 : 1. After the final accounts have been prepared, it was discovered that interest on drawings had not been taken into consideration. The interest on drawing of partners amounted to *X* ₹2,550, *Y* ₹1,850 and *Z* ₹1,000. Give the necessary adjusting journal entry.

SOLUTION :

Interest charged on *X*'s drawings	=	₹2,550
Interest charged on *Y*'s drawings	=	₹1,850
Interest charged on *Z*'s drawings	=	₹1,000
Total interest to be charged from partners		₹5,400

This amount of ₹5,400 is an item of income for the firm but this has not been recorded on the credit side of P & L App. A/c of the previous year. As such the profit of the previous year will now be increased by this amount. Hence, this profit of ₹5,400 will be shared by the partners in their profit sharing ratio of 3 : 2 : 1 which amounts to *X* ₹2700, *Y* ₹1,800 and *Z* ₹900.

TABLE SHOWING ADJUSTMENT

		X	Y	Z	Total
		₹	₹	₹	₹
Interest on Drawings	(Dr.)	2,550	1,850	1,000	5,400
Division of ₹5,400 in 3 : 2 : 1	(Cr.)	2,700	1,800	900	5,400
Difference		Cr. 150	Dr. 50	Dr. 100	—

Hence the adjusting entry will be :

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Date	Particulars		L.F.	Dr. ₹	Cr. ₹
	Y's Capital A/c	Dr.		50	
	Z's Capital A/c	Dr.		100	
	To X's Capital A/c				150
	(Adjustment in respect of interest on drawing omitted in previous year's accounts)				

ILLUSTRATION 44.

X, Y and *Z* are partners sharing profits and losses in the ratio of 3 : 2 : 1. After the final accounts have been prepared, it was discovered that interest on drawings @ 5% p.a. had not been taken into consideration. The drawings of the Partners were : *X* ₹1,50,000; *Y* ₹1,26,000; *Z* ₹1,20,000. Give the necessary adjusting journal entry.

SOLUTION :

Calculation of Interest on Drawings :

Since date of drawings are not given, interest will be charged for 6 months.

		₹
X : 5% on ₹1,50,000 for 6 months	=	3,750
Y : 5% on ₹1,26,000 for 6 months	=	3,150
Z : 5% on ₹1,20,000 for 6 months	=	3,000
		9,900

TABLE SHOWING ADJUSTMENT

		X	Y	Z	Total
		₹	₹	₹	₹
Interest on Drawings	(Dr.)	3,750	3,150	3,000	9,900
Division of ₹9,900 in 3 : 2 : 1	(Cr.)	4,950	3,300	1,650	9,900
Difference		Cr. 1,200	Cr. 150	Dr. 1,350	—

JOURNAL ENTRY

Date	Particulars		L.F.	Dr. ₹	Cr. ₹
	Z's Capital A/c	Dr.		1,350	
	To X's Capital A/c				1,200
	To Y's Capital A/c				150
	(Adjustment of omission of interest on drawings)				

ILLUSTRATION 45.

R and *S* were partners in a firm sharing profits in 3 : 2 ratio. Their respective fixed capitals were ₹10,00,000 and ₹15,00,000. The partnership deed provided the following :

(*i*) Interest on capital @ 10% p.a.

(*ii*) Interest on drawing @ 12% p.a.

During the year ended 31-3-2020, *R*'s drawings were ₹10,000 per month drawn at the end of every month and *S*'s drawings were ₹20,000 per month drawn in the beginning of the every month. After the preparation of final accounts for the year ended 31-3-2020 it was discovered that interest on *R*'s drawings was not taken into consideration.

Calculate interest on *R*'s drawings and give necessary adjusting entry for the same.

SOLUTION :

Calculation of Interest on *R*'s Drawings :

Total drawings for the year = ₹10,000 × 12 = ₹1,20,000.

When equal amount is withdrawn at the end of every month, interest is calculated for an average period of $5\frac{1}{2}$ months :

$$\text{Interest on Drawings} = 1{,}20{,}000 \times \frac{12}{100} \times \frac{5.5}{12} = ₹6{,}600$$

TABLE SHOWING ADJUSTMENT

		R	*S*	*Total*
		₹	₹	₹
Interest on Drawings	(Dr.)	6,600		6,600
Division of ₹6,600 in 3 : 2	(Cr.)	3,960	2,640	6,600
Difference		Dr. 2,640	Cr. 2,640	—

ADJUSTMENT ENTRY

Date	*Particulars*		*L.F.*	*Dr.* ₹	*Cr.* ₹
2020					
April 1	*R*'s Current A/c	Dr.		2,640	
	To *S*'s Current A/c				2,640
	(Adjustment of omission of interest on drawings)				

ILLUSTRATION 46.

L, *M* and *N* partners have omitted interest on capitals for three years ended on 31st March, 2020. Their fixed capitals in three years were *L* ₹40,000, *M* ₹25,000, *N* ₹15,000. Rate of interest on capital is 12% p.a.Their profit sharing ratios were 2018 — 5 : 2 : 1, 2019 — 3 : 2 : 1, 2020 — 2 : 1 : 1. Give the necessary adjusting entry.

SOLUTION :

TABLE SHOWING ADJUSTMENT

	L	M	N	Total
	Cr. (₹)	Cr. (₹)	Cr. (₹)	(₹)
Interest on Capitals @ 12% p.a.				
I for the year 2018	4,800	3,000	1,800	9,600
II for the year 2019	4,800	3,000	1,800	9,600
III for the year 2020	4,800	3,000	1,800	9,600
Total Amount Payable (Cr.)	14,400	9,000	5,400	28,800
Division of Firm's loss will be as under :	Dr. (₹)	Dr. (₹)	Dr. (₹)	(₹)
I for the year 2018 in the ratio of 5 : 2 : 1	6,000	2,400	1,200	9,600
II for the year 2019 in the ratio of 3 : 2 : 1	4,800	3,200	1,600	9,600
III for the year 2020 in the ratio of 2 : 1 : 1	4,800	2,400	2,400	9,600
Total Loss (Dr.)	15,600	8,000	5,200	28,800

Date	*Particulars*	*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2020				
April 1	*L*'s Current A/c Dr. 15,600 – 14,400		1,200	
	To *M*'s Current A/c 9,000 – 8,000			1,000
	To *N*'s Current A/c 5,400 – 5,200			200
	(Adjustment for the omission of three years' interest on capitals)			

ILLUSTRATION 47.

Mudit and Uday are partners in a firm sharing profits in the ratio 2 : 3. Their capital accounts as on April 1, 2021 showed balances of ₹70,000 and ₹60,000 respectively. The drawings of Mudit and Uday during the year 2021-22 were ₹16,000 and ₹12,000 respectively. Both the amounts were withdrawn on 1st January 2022. It was subsequently found that the following items had been omitted while preparing the final accounts for the year ended 31st march 2022.

(*a*) Interest on capitals @ 6% p.a.;

(*b*) Interest on drawings @ 6% p.a.;

(*c*) Mudit was entitled to a commission of ₹4,000 for the whole year.

Showing your workings clearly pass a rectifying entry in the books of the firm.

SOLUTION :

Particulars		*Mudit*	*Uday*	*Total*
		₹	₹	₹
Interest on Capital	(Cr.)	4,200	3,600	7,800
Commission	(Cr.)	4,000		4,000
		8,200	3,600	11,800
Less : Interest on Drawings (for 3 months)	(Dr.)	240	180	420
		7,960	3,420	11,380

Less : Division of Firm's Loss of ₹11,380 in 2 : 3	(Dr.)	4,552	6,828	11,380
Net Effect		(Cr.) 3,408	(Dr.) 3,408	

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Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
2022				₹	₹
April 1	Uday's Capital A/c	Dr.		3,408	
	To Mudit's Capital A/c				3,408
	(Rectifying entry for omissions)				

ILLUSTRATION 48.

The net profit of a firm for the year ended 31st March, 2022, was ₹30,000, which has been duly distributed amongst its three partners *A, B* and *C* in their agreed proportions of 3 : 1 : 1 respectively. It was discovered on 10th April, 2022 that the undermentioned transactions were not passed through the books of accounts of the firm for the year ended 31st March, 2022, which stood duly closed on that date :

(*a*) Interest on capital at 10% p.a.
(*b*) Interest on drawings : *A* ₹350; *B* ₹250; *C* ₹150.
(*c*) Salary of ₹5,000 to *A* and ₹7,500 to *B*.
(*d*) Commission due to *A* on a special transaction, ₹3,000.

The capital accounts of the partners on 1st April, 2021 were : *A* ₹25,000; *B* ₹20,000; *C* ₹15,000.

You are required to suggest a journal entry to be passed on 10th April, 2022 which will not affect the Profit and Loss Appropriation Account of the firm for the year ended 31st March, 2022 and at the same time will rectify the position of the partners.

SOLUTION :

		A	*B*	*C*	*Total*
		₹	₹	₹	₹
Interest on Capital	(Cr.)	2,500	2,000	1,500	6,000
Salary	(Cr.)	5,000	7,500	—	12,500
Commission	(Cr.)	3,000	—		3,000
		10,500	9,500	1,500	21,500
Less : Interest on Drawings	(Dr.)	350	250	150	750
		10,150	9,250	1,350	20,750
Division of Firm's Loss of ₹20,750 in 3 : 1 : 1	(Dr.)	12,450	4,150	4,150	
Net Effect		(Dr.) 2,300	(Cr.) 5,100	(Dr.) 2,800	

Adjustment Entry :—

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022 April 10	*A*'s Capital A/c	Dr.		2,300	
	C's Capital A/c	Dr.		2,800	
	To *B*'s Capital A/c				5,100
	(Adjustment for omissions)				

ILLUSTRATION 49.

Praveen, Sahil and Riya are partners having fixed capitals of ₹2,00,000, ₹1,60,000 and ₹1,20,000 respectively. They share profits in the ratio of 3 : 1 : 1. The Partnership Deed provided for the following which were not recorded in the books :

(*i*) Interest on Capital @5% p.a.

(*ii*) Salary to Praveen ₹1,500 p.m. and to Riya ₹1,000 p.m.

(*iii*) Transfer of profit to General Reserve ₹10,000. Net Profit for the year ended 31st March, 2022 distributed among the partners was ₹1,00,000.

Pass necessary rectifying entry for the above adjustments in the books of the firm. Also show your workings clearly.

SOLUTION : TABLE SHOWING ADJUSTMENTS

		Praveen ₹	Sahil ₹	Riya ₹	Total ₹
Interest on Capital	(Cr.)	10,000	8,000	6,000	24,000
Salary	(Cr.)	18,000		12,000	30,000
Total Amount Payable	(Cr.)	28,000	8,000	18,000	54,000
Division of firm's loss of ₹54,000 in 3 : 1 : 1	(Dr.)	32,400	10,800	10,800	54,000
		(Dr.) 4,400	(Dr.) 2,800	(Cr.) 7,200	—
Adjustment for Transfer to General Reserve : ₹10,000 in 3 : 1 : 1		(Dr.) 6,000	(Dr.) 2,000	(Dr.) 2,000	(Cr.) 10,000
Net Effect		(Dr.) 10,400	(Dr.) 4,800	(Cr.) 5,200	(Cr.) 10,000

Rectifying Entry :—

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022 April 1	Praveen's Current A/c	Dr.		10,400	
	Sahil's Current A/c	Dr.		4,800	
	To Riya's Current A/c				5,200
	To General Reserve A/c				10,000
	(Adjustments for the omission of interest on capital, salary and transfer to General Reserve)				

ILLUSTRATION 50.

Rohit, Raman and Raina are partners in a firm. Their capital accounts on 1st April, 2019, stood at ₹2,00,000, ₹1,20,000 and ₹1,60,000 respectively. Each partner

withdrew ₹15,000 during the financial year 2019-20.

As per the provisions of their partnership deed :

(a) Interest on capital was to be allowed @5% per annum.

(b) Interest on drawings was to be charged @4% per annum.

(c) Profits and losses were to be shared in the ratio 5 : 4 : 1.

The net profit of ₹72,000 for the year ended 31st March 2020, was divided equally amongst the partners without providing for the terms of the deed.

You are required to pass a single adjustment entry to rectify the error (show workings clearly). *(C.B.S.E. Sample Paper 2020)*

SOLUTION:

Adjustment Table

Particulars		*Rohit*	*Raman*	*Raina*	*Firm*
		₹	₹	₹	₹
Interest on Capitals	(Cr.)	10,000	6,000	8,000	24,000
Interest on Drawings	(Dr.)	300	300	300	900
Remaining Profit* : ₹72,000 – ₹24,000 + ₹900 = ₹48,900 divided in 5 : 4 : 1	(Cr.)	24,450	19,560	4,890	48,900
Net amount which should have been credited	(Cr.)	34,150	25,260	12,590	72,000
Less : Profit already distributed equally	(Dr.)	24,000	24,000	24,000	72,000
		10,150 (Cr.)	1,260 (Cr.)	11,410 Dr.	—

* Remaining profit will have to be calculated when profit has already been distributed in wrong profit sharing ratio.

ADJUSTMENT ENTRY

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2020					
April 1	Raina's Capital A/c	Dr.		11,410	
	To Rohit's Capital A/c				10,150
	To Raman's Capital A/c				1,260
	(Adjustment entry passed for omissions)				

ILLUSTRATION 51.

X, *Y* and *Z* were partners in a firm. On 1st April, 2019 their capitals stood at ₹6,00,000, ₹4,00,000 and ₹2,00,000 respectively. As per provisions of the partnership deed :

(*i*) *Y* was entitled for commission of ₹12,000 p.a.

(*ii*) *X* was entitled for a salary of ₹1,200 per month.

(*iii*) Partners were entitled to interest on Capital @ 8% p.a.

(*iv*) Profits were to be shared in the ratio of Capitals.

Net profit for the year ended 31.03.2020 was ₹4,22,400 which was distributed equally, without taking into consideration the above provisions. Showing your workings clearly, pass necessary adjustment entry for the above.

SOLUTION :

	X ₹	Y ₹	Z ₹	Total ₹
Commission to *Y* (Cr.)		12,000		12,000
Salary to *X* (Cr.)	14,400			14,400
Interest on Capital (Cr.)	48,000	32,000	16,000	96,000
Profit remaining after allowing commission, salary and interest on capital will be ₹4,22,400 – ₹12,000 – ₹14,400 – ₹96,000 = ₹3,00,000. It will be divided in their profit sharing ratio, *i.e.*, 3 : 2 : 1.	1,50,000	1,00,000	50,000	3,00,000
Net amount which should have been received (Cr.)	2,12,400	1,44,000	66,000	4,22,400
Less : Profit already distributed equally (Dr.)	1,40,800	1,40,800	1,40,800	4,22,400
	71,600 (Cr.)	3,200 (Cr.)	74,800 (Dr.)	—

ADJUSTMENT ENTRY

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2020					
April 1	*Z*'s Capital A/c	Dr.		74,800	
	To *X*'s Capital A/c				71,600
	To *Y*'s Capital A/c				3,200
	(Adjustment for commission, salary, interest on capital and wrong distribution of profit)				

ILLUSTRATION 52.

A, *B* and *C* were partners. Their capitals were ₹30,000; ₹20,000 and ₹10,000 respectively on 1st April, 2019. According to the partnership deed they were entitled to an interest on capital at 5% p.a. In addition *B* was also entitled to draw a salary of ₹500 per month. *C* was entitled to a commission of 5% on the profits after charging the interest on capital, but before charging the salary payable to *B*. The net profits for the year ended 31st March, 2020 were ₹30,000, distributed in the ratio of their capitals without providing for any of the above adjustments. The profits were to be shared in the ratio of 2 : 2 : 1. Pass the necessary adjustment entry showing the workings clearly.

SOLUTION :

STATEMENT OF ADJUSTMENT

	A ₹	B ₹	C ₹	Total ₹
Interest on Capital	1,500	1,000	500	3,000
Salary (₹500 × 12)		6,000		6,000

Commission : 5% on (30,000 – Interest on Capital 3,000)			1,350	1,350
Remaining Profit *i.e.* ₹30,000 – ₹3,000 – ₹6,000 – ₹1,350 = ₹19,650 will be divided in their profit sharing ratio *i.e.* 2:2:1	7,860	7,860	3,930	19,650
Net amount which should have been received (Cr.)	9,360	14,860	5,780	30,000
Less : Profit already distributed in 3 : 2 : 1 (Dr.)	15,000	10,000	5,000	30,000
Net Effect	(Dr.) 5,640	(Cr.) 4,860	(Cr.) 780	—

ADJUSTMENT ENTRY

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2020 April 1	*A*'s Capital A/c	Dr.		5,640	
	To *B*'s Capital A/c				4,860
	To *C*'s Capital A/c				780
	(Adjustment for omissions)				

ILLUSTRATION 53.

The partners of a firm distributed the profits for the year ended 31st March, 2020, ₹90,000 in the ratio of 3 : 2 : 1 without providing for the following adjustments :

(*i*) *A* and *B* were entitled to a salary of ₹1,500 each per annum.

(*ii*) *B* was entitled to a commission of ₹4,500.

(*iii*) *B* and *C* had guaranteed a minimum profit of ₹35,000 p.a. to *A*.

(*iv*) Profits were to be shared in the ratio of 3 : 3 : 2.

Pass necessary journal entry for the above adjustments in the books of the firm.

SOLUTION : TABLE SHOWING ADJUSTMENT

	A ₹	*B* ₹	*C* ₹	*Total* ₹
Salary (Cr.)	1,500	1,500		3,000
Commission (Cr.)		4,500		4,500
Profit guaranteed to *A* (Cr.)[(1)]	35,000			35,000
Remaining Profit, *i.e.*, ₹90,000 – ₹3,000 – ₹4,500 – ₹35,000 = ₹47,500 will be divided between *B* and *C* in 3 : 2 (Cr.)		28,500	19,000	47,500
(Cr.)	36,500	34,500	19,000	90,000
Less : Profit already distributed (₹90,000 in 3 : 2 : 1) (Dr.)	45,000	30,000	15,000	90,000
Net Effect	(Dr.) 8,500	(Cr.) 4,500	(Cr.) 4,000	—

ADJUSTMENT ENTRY

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2020					
April 1	A's Capital A/c	Dr.		8,500	
	To B's Capital A/c				4,500
	To C's Capital A/c				4,000
	(Adjustment for omissions)				

Working Note (1)

Profit remaining after allowing salary and commission will be :
₹90,000 – ₹3,000 – ₹4,500 = ₹82,500

A's share = 82,500 × $\frac{3}{8}$ = ₹30,938

Since it is less than guaranteed amount of ₹35,000, he will be allowed ₹35,000.

ILLUSTRATION 54.

Rajeev and Sanjeev were partners in a firm. Their partnership deed provided that the profits shall be divided as follows :

First ₹20,000 to Rajeev and the balance in the ratio of 4 : 1. The profits for the year ended 31st March, 2022 were ₹60,000 which had been distributed among the partners. On 1-4-2021 their capitals were Rajeev ₹90,000 and Sanjeev ₹80,000. Interest on capital was to be provided @6% p.a. While preparing the profit and loss appropriation interest on capital was omitted.

Pass necessary rectifying entry for the same. Show your workings clearly.

SOLUTION :

STATEMENT OF ADJUSTMENTS

Particulars	Rajeev	Sanjeev	Total
	₹	₹	₹
Interest on Capital	(Cr.) 5,400	4,800	10,200
Profit remaining after interest on Capital : ₹60,000 – ₹10,200 = ₹49,800.			
First 20,000 to Rajeev	(Cr.) 20,000		20,000
Remaining ₹29,800 (₹49,800 – 20,000) in the ratio of 4 : 1	(Cr.) 23,840	5,960	29,800
	(Cr.) 49,240	10,760	60,000
Less : Profit already distributed	(Dr.) 20,000		20,000
Remaining 40,000 (₹60,000 – 20,000) in the ratio of 4 : 1	(Dr.) 32,000	8,000	40,000
	(Dr.) 2,760	(Cr.) 2,760	—

Books of Rajeev and Sanjeev
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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022 April 1	Rajeev's Capital A/c	Dr.		2,760	
	To Sanjeev's Capital A/c				2,760
	(Adjustment for omission of interest on capital)				

ILLUSTRATION 55.
(Rectification of Interest on Capital less charged)

P, Q and *R* are partners in a firm sharing profits and losses in the ratio of 2 : 1 : 2. Their **fixed capitals** were ₹3,00,000; ₹1,00,000 and ₹2,00,000 respectively. Interest on capital for the year ended 31st March, 2021 was credited to them @ 9% p.a. instead of 12% p.a. The profit for the year before charging interest was ₹2,50,000. Prepare necessary adjustment entry.

SOLUTION :

Interest on capital has been credited @9% instead of 12%. Hence, additional interest of 3% will be credited to partners.

TABLE SHOWING ADJUSTMENT

	P ₹	*Q* ₹	*R* ₹	*Total* ₹
Partners less credited with 3% interest	9,000	3,000	6,000	18,000
By allowing this interest, the profits of the firm will be reduced by ₹18,000. This loss will be divided in the ratio of 2 : 1 : 2.	7,200	3,600	7,200	18,000
Net effect	(Cr.) 1,800	(Dr.) 600	(Dr.) 1,200	—

Adjustment Entry :—

Date	Particulars		L.F.	Dr. ₹	Cr. ₹
2021 April 1	*Q*'s Current A/c	Dr.		600	
	R's Current A/c	Dr.		1,200	
	To *P*'s Current A/c				1,800
	(Interest less charged on capital, now rectified)				

ILLUSTRATION 56.
(Rectification of excessive interest on capital)

A, B and *C* are partners in a firm sharing profits and losses in the ratio of 2 : 3 : 5. Their **fixed capitals** were ₹15,00,000, ₹30,00,000 and ₹60,00,000 respectively. For the year ended 31st March, 2022 interest on capital was credited to them @ 12% instead of 10%. Pass the necessary adjustment entry.

SOLUTION :

TABLE SHOWING ADJUSTMENT

	A ₹	*B* ₹	*C* ₹	*Total* ₹
Partners Over credited with 2% interest	30,000	60,000	1,20,000	2,10,000
By recovering this interest from the partners, the profits of the firm will be increased by ₹2,10,000. This profit will be divided in the ratio of 2 : 3 : 5	42,000	63,000	1,05,000	2,10,000
Net effect	12,000 (Cr.)	3,000 (Cr.)	15,000 (Dr.)	—

ADJUSTMENT ENTRY

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2022 April 1	*C*'s Current A/c	Dr.		15,000	
	To *A*'s Current A/c				12,000
	To *B*'s Current A/c				3,000
	(Interest excessive charged, now rectified)				

ILLUSTRATION 57.

(Interest on Drawings wrongly provided)

Ram, Mohan and Sohan were partners sharing profits in the ratio of 2 : 1 : 1. Ram withdrew ₹3,000 every month and Mohan withdrew ₹4,000 every month. Interest on drawings @ 6% p.a. was charged, whereas the partnership deed was silent about interest on drawings.

Showing your working clearly, pass the necessary adjustment entry to rectify the error. *(C.B.S.E. 2020; Delhi)*

SOLUTION :

Calculation of Interest on Drawings :

Ram : $36,000 \times \frac{6}{100} \times \frac{6}{12} = ₹1,080$

Mohan : $48,000 \times \frac{6}{100} \times \frac{6}{12} = ₹1,440$

TABLE SHOWING ADJUSTMENT

		Ram ₹	*Mohan* ₹	*Sohan* ₹	*Total* ₹
Cancellation of Interest on Drawings	(Cr.)	1,080	1,440	-	2,520
Division of ₹2,520 in 2 : 1 : 1	(Dr.)	1,260	630	630	2,520
Net effect		Dr. 180	Cr. 810	Dr. 630	—

ADJUSTMENT ENTRY

Date	Particulars		L.F.	Dr. ₹	Cr. ₹
	Ram's Capital A/c	Dr.		180	
	Sohan's Capital A/c	Dr.		630	
	To Mohan's Capital A/c				810
	(Adjustment for interest on drawings wrongly charged)				

ILLUSTRATION 58.

A, B and *C* are partners in a firm. After the accounts of partnership have been drawn up and the books closed off, it is discovered that for the years ended 31st March 2016 and 2017, interest has been allowed to the partners upon their Capitals @ 6% p.a. although there is no provision for interest in the partnership deed. Their fixed capitals on which interest was calculated were ₹1,00,000; ₹80,000 and ₹60,000 respectively.

During the last two years, they have shared the profits as follows :—

2016 3 : 2 : 1
2017 5 : 3 : 2

You are required to give necessary adjusting entry on 1st April, 2017.

(C.B.S.E. Sample Paper, 2017)

SOLUTION : TABLE SHOWING ADJUSTMENT

	A ₹	*B* ₹	*C* ₹	*Total* ₹
Cancellation of Interest on Capitals @ 6% p.a.	Dr.	Dr.	Dr.	
For the year 2016	6,000	4,800	3,600	14,400
For the year 2017	6,000	4,800	3,600	14,400
Total amount recoverable from partners (Dr.)	12,000	9,600	7,200	28,800
Division of firm's profit will be as under :	Cr.	Cr.	Cr.	
For the year 2016 in the ratio of 3 : 2 : 1	7,200	4,800	2,400	14,400
For the year 2017 in the ratio of 5 : 3 : 2	7,200	4,320	2,880	14,400
Total profit distributed among partners (Cr.)	14,400	9,120	5,280	28,800
Net Effect	Cr. 2,400	Dr. 480	Dr. 1,920	

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Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2017 April 1	*B*'s Current A/c 9,600 – 9,120	Dr.		480	
	C's Current A/c 7,200 – 5,280	Dr.		1,920	
	To *A*'s Current A/c 14,400 – 12,000				2,400
	(Interest on capital wrongly provided in the accounts for two years, now adjusted.)				

ILLUSTRATION 59.

X, Y and *Z* have been sharing profits in the ratio of 2 : 2 : 1 respectively. *Z* wants that he should be given equal share in profits with *X* and *Y* and he further wants that the

change in the profits sharing ratio should come into effect retrospectively for the last three years. X and Y have no objection to this. The profit for last three years were, ₹52,000, ₹44,200 and ₹51,610.

Show the adjustment of profit for the last three years by means of a Journal entry.

SOLUTION :

TABLE SHOWING ADJUSTMENTS

	X ₹	Y ₹	Z ₹
Total Profits for three years 52,000 + 44,200 + 51,610 = 1,47,810 This Profit has already been divided in the ratio of 2 : 2 : 1	59,124	59,124	29,562
If Profits are shared equally : $\frac{1,47,810}{3} = 49,270$	49,270	49,270	49,270
Net Effect	Dr. 9,854	Dr. 9,854	Cr. 19,708

It is clear from the above table that X and Y, both have received ₹59,124 each, whereas each one of them should have received only ₹49,270 each. Therefore, X and Y will surrender ₹9,854 each in favour of Z.

Following adjustment entry will be passed for this purpose :

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	X's Capital A/c	Dr.		9,854	
	Y's Capital A/c	Dr.		9,854	
	To Z's Capital A/c				19,708
	(Excess amount paid to X and Y now corrected)				

ILLUSTRATION 60.

On March 31, 2022 the capital accounts of Elvin, Monu and Ahmed after making adjustments for profits, drawings, etc. were as, Elvin — ₹80,000; Monu — ₹60,000; and Ahmed — ₹40,000. Subsequently, it was discovered that interest on capital and interest on drawings had been omitted. The partners were entitled to interest on capital @ 5% p.a. The drawings during the year were : Elvin — ₹20,000; Monu — ₹15,000; and Ahmed — ₹9,000. Interest on drawings chargeable to the partners was Elvin — ₹500; Monu — ₹360 and Ahmed — ₹200. The net profit for the year ended 31st March, 2022 amounted to ₹1,20,000. The profit sharing ratio of the partners was 3 : 2 : 1.

Record the necessary adjustment entry for rectifying the above errors of omission. Show your workings.

SOLUTION :

Since interest on capitals is always calculated on opening capitals and the same have not been given, first of all, it is necessary to calculate the opening capitals :

Particulars	Elvin ₹	Monu ₹	Ahmed ₹
Capitals as on 31.3.2022	80,000	60,000	40,000

Less : Share of Profit (Which has already been added) 1,20,000 shared in the ratio of 3 : 2 : 1	60,000	40,000	20,000
	20,000	20,000	20,000
Add : Drawings (Which were previously deducted)	20,000	15,000	9,000
Capitals as on 1.4.2021	40,000	35,000	29,000

Interest on Capital :

Elvin 5% on ₹40,000 = ₹2,000

Monu 5% on ₹35,000 = ₹1,750

Ahmed 5% on ₹29,000 = ₹1,450

TABLE SHOWING ADJUSTMENT

Particulars	*Elvin*	*Monu*	*Ahmed*	*Total*
	₹	₹	₹	₹
Interest on Opening Capitals	2,000	1,750	1,450	5,200
Less : Interest on Drawings	(–) 500	(–) 360	(–) 200	(–) 1,060
Balance (Cr.)	1,500	1,390	1,250	4,140
Division of Firm's loss of ₹4,140 in the ratio of 3 : 2 : 1 (Dr.)	(–) 2,070	(–) 1,380	(–) 690	
	(Dr.) 570	(Cr.) 10	(Cr.) 560	

Adjusting Entry :—

Date	*Particulars*	*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2022				
April 1	Elvin's Capital A/c Dr.		570	
	To Monu's Capital A/c			10
	To Ahmed's Capital A/c			560
	(The adjustment on account of the omission of the interest on capitals and drawings)			

ILLUSTRATION 61.

(Omission of Interest on capital when fixed capitals are given.)

Assuming the capitals were fixed in Illustration 60, give the necessary adjusting journal entry.

SOLUTION :

	Elvin	*Monu*	*Ahmed*
	₹	₹	₹
Interest on Capital @ 5% p.a.	4,000	3,000	2,000

STATEMENT SHOWING THE ADJUSTMENT TO BE MADE

Particulars	*Elvin*	*Monu*	*Ahmed*	*Total*
	₹	₹	₹	₹
Interest on Capitals	4,000	3,000	2,000	9,000

Less : Interest on drawings	(–) 500	(–) 360	(–) 200	(–) 1,060
(Cr.)	3,500	2,640	1,800	7,940
Division of firm's loss of ₹7,940 in the ratio of 3 : 2 : 1 (Dr.)	(–) 3,970	(–) 2,647	(–) 1,323	
	(Dr.) 470	(Dr.) 7	(Cr.) 477	

Adjusted Entry :

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
April 1	Elvin's Current A/c	Dr.		470	
	Monu's Current A/c	Dr.		7	
	To Ahmed's Current A/c				477
	(Adjustment on account of omission of the interest on capitals and drawings in the accounts)				

ILLUSTRATION 62.

On 31st March, 2022, the balances in the Capital Accounts of *A*, *B* and *C* after making adjustments for profits and drawings were ₹1,60,000, ₹1,20,000 and ₹80,000 respectively. Subsequently, it was discovered that the interest on capital and drawings had been omitted.

- The profit for the year ended 31st March, 2022 was ₹40,000.
- During the year, *A* and *B* each withdrew a total sum of ₹24,000 in equal instalments in the beginning of each month and *C* withdrew a total sum of ₹48,000 in equal instalments at the end of each month.
- The interest on drawings was to be charged @5% p.a. and interest on capital was to be allowed @10% p.a.
- The profit-sharing ratio among the partners was 2 : 1 : 1.

Showing your working notes clearly, pass the necessary rectifying entry.

SOLUTION :

Particulars	A ₹	B ₹	C ₹
Closing Capitals as on 31.3.2022	1,60,000	1,20,000	80,000
Less : Share of Profit (already credited ₹40,000 shared in the ratio of 2 : 1 : 1)	20,000	10,000	10,000
	1,40,000	1,10,000	70,000
Add : Drawings (already debited)	24,000	24,000	48,000
Opening Capitals as on 1.4.2021	1,64,000	1,34,000	1,18,000

Interest on Capital :

A : 10% on 1,64,000	=	16,400
B : 10% on 1,34,000	=	13,400
C : 10% on 1,18,000	=	11,800
Total Interest on Capital		41,600

Interest on Drawings :

$$A = 24{,}000 \times \frac{5}{100} \times \frac{6.5}{12} = ₹\ 650$$

$$B = 24{,}000 \times \frac{5}{100} \times \frac{6.5}{12} = ₹\ 650$$

$$C = 48{,}000 \times \frac{5}{100} \times \frac{5.5}{12} = ₹1{,}100$$

Total Interest on Drawings 2,400

TABLE SHOWING ADJUSTMENT

Particulars		*A*	*B*	*C*	*Total*
		₹	₹	₹	₹
Interest on Opening Capitals		16,400	13,400	11,800	41,600
Less : Interest on Drawings		650	650	1,100	2,400
Balance	(Cr.)	15,750	12,750	10,700	39,200
Division on Firm's loss of ₹39,200 in the ratio of 2 : 1 : 1	(Dr.)	19,600	9,800	9,800	39,200
		Dr. 3,850	Cr. 2,950	Cr. 900	—

Rectifying Entry :

Date	*Particulars*		*L.F.*	Dr. ₹	Cr. ₹
2022					
March 31	*A*'s Capital A/c	Dr.		3,850	
	To *B*'s Capital A/c				2,950
	To *C*'s Capital A/c				900
	(The adjustment on account of the omission of the interest on capitals and drawings)				

ILLUSTRATION 63.

The capital accounts of Alka and Archana showed credit balances of ₹4,00,000 and ₹3,00,000 respectively, after taking into account drawings and net profit of ₹2,00,000. The drawings of the partners during the year 2018-19 were :

(*i*) Alka withdrew ₹10,000 at the end of each quarter.

(*ii*) Archana's drawings were :

	₹
31st May, 2018	8,000
1st November, 2018	7,000
1st February, 2019	5,000

Calculate interest on partners' capitals @ 10% p.a. and interest on partners' drawings @ 6% p.a. for the year ended 31st March, 2019.

(C.B.S.E. 2020, Kolkata, Lucknow)

SOLUTION :

Calculation of Opening Capitals :

Particulars	*Alka*	*Archana*
	₹	₹
Closing Capitals	4,00,000	3,00,000
Add : Drawings	40,000	20,000
Less : Profits (₹2,00,000 in 1 : 1)	(1,00,000)	(1,00,000)
Opening Capitals	3,40,000	2,20,000
Interest on Capital @ 10% p.a.	34,000	22,000

Interest on Drawings :

Alka's Interest on Drawings = $40,000 \times \frac{6}{100} \times \frac{4.5}{12}$ = ₹900

Archana's Interest on Drawings :

Date	*Amount of Drawings (₹)*	*No. of months upto 31st March 2019*	*Products (₹)*
31.5.2018	8,000	10	80,000
1.11.2018	7,000	5	35,000
1.2.2019	5,000	2	10,000
			1,25,000

Archana's Interest on Drawings = $1,25,000 \times \frac{6}{100} \times \frac{1}{12}$ = ₹625

ILLUSTRATION 64.

Puneet and Akshara were partners in a firm sharing profits and losses in the ratio of 2 : 3. The following was the balance sheet of the firm as at 31st March, 2019.

Balance Sheet of Puneet and Akshara as at 31st March, 2019

Liabilities		₹	*Assets*	₹
Capitals :			Sundry Assets	2,00,000
Puneet	90,000			
Akshara	1,10,000	2,00,000		
		2,00,000		2,00,000

The profits ₹40,000 for the year ended 31st March, 2019 were divided between the partners without allowing interest on capital @5% p.a. and commission to Akshara @₹1,000 per quarter.

The drawings of the partners during the year were :

Puneet ₹2,500 per month.

Akshara ₹10,000 per quarter.

Showing your workings clearly, pass necessary adjustment entry in the books of the firm. *(C.B.S.E. 2020, Delhi)*

SOLUTION :

Books of Puneet and Akshara

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Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2019 April 1	Puneet's Capital A/c Dr. To Akshara's Capital A/c (Rectifying entry for omission of Interest on Capital and Akshara's commission)		1,000	1,000

Working Notes :

(1) Calculation of Opening Capitals :

Particulars	Puneet	Akshara
	₹	₹
Closing Capitals	90,000	1,10,000
Add : Drawings	30,000	40,000
	1,20,000	1,50,000
Less : Profit (₹40,000 in 2 : 3)	16,000	24,000
Opening Capitals	1,04,000	1,26,000
Interest on Capitals @5%	5,200	6,300

(2) Past Adjustment Table :

Particulars		Puneet	Akshara	Total
		₹	₹	₹
Omission of Interest on Capital (5%)		5,200	6,300	11,500
Omission of Commission to Akshara			4,000	4,000
	(Cr.)	5,200	10,300	15,500
₹15,500 divided in 2 : 3	(Dr.)	6,200	9,300	15,500
Net Effect	(Dr.)	1,000	Cr. 1,000	—

ILLUSTRATION 65.

Himanshu and Vikrant are partners in a firm and share profits equally. Their Balance Sheet as at March 31, 2017 is as follows :

BALANCE SHEET
as at March 31, 2017

Liabilities		Amount	Assets	Amount
		₹		₹
Capitals :			Fixed Assets	3,60,000
Himanshu	2,00,000		Current Assets	40,000
Vikrant	1,40,000	3,40,000		
Creditors		60,000		
		4,00,000		4,00,000

During the year 2016-17, Himanshu's Drawings were ₹30,000 and Vikrant's Drawings were ₹40,000. During the year 2016-17 the firm earned profit of ₹1,00,000. While distributing profits for the year 2016-17, interest on capital @ 5% per annum and interest on drawings @ 12% per annum were ignored.

Showing your workings clearly, pass necessary rectifying entry.

(C.B.S.E. Sample Paper, 2018)

SOLUTION : Calculation of Opening Capitals

Particulars	*Himanshu*	*Vikrant*
	₹	₹
Closing Capitals	2,00,000	1,40,000
Add : Drawings	30,000	40,000
	2,30,000	1,80,000
Less : Profit already Distributed (₹1,00,000 in equal proportion)	50,000	50,000
Opening Capitals	1,80,000	1,30,000

Table Showing Adjustment :

	Particulars		*Himanshu*	*Vikrant*	*Total*
			₹	₹	₹
	Interest on Capital (5% on Opening Capitals)	(Cr.)	9,000	6,500	15,500
Less :	Interest on Drawings (12% p.a. for half year)	(Dr.)	1,800	2,400	4,200
			7,200	4,100	11,300
Less :	Division of Firm's loss of ₹11,300 equally	(Dr.)	5,650	5,650	11,300
Net Effect			(Cr.) 1,550	(Dr.) 1,550	—

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Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
				₹	₹
2017 April 1	Vikrant's Capital A/c	Dr.		1,550	
	To Himanshu's Capital A/c				1,550
	(Adjustment for omission of interest on capital and interest on drawings)				

ILLUSTRATION 66.

Mannu and Shristhi are partners in a firm sharing profits in the ratio of 3 : 2. Following is the balance sheet of the firm as at 31st March, 2022 :

Liabilities		₹	*Assets*		₹
Mannu's Capital	3,00,000		Drawings :		
Shristhi's Capital	1,00,000	4,00,000	Mannu	40,000	
			Shristhi	20,000	60,000

		Other Assets	3,40,000
	4,00,000		4,00,000

Profit for the year ending 31st March, 2022 ₹50,000 was divided between the partners in the agreed ratio, but interest on capital at 5% p.a. and on drawings at 6% p.a. was inadvertently ignored. Adjust interest on drawings on an average basis for 6 months. Give the adjustment entry. *(NCERT, Modified)*

SOLUTION:

	Mannu	*Shristhi*
	₹	₹
Closing Capitals	3,00,000	1,00,000
Less : Share of profit (₹50,000 in 3 : 2)	30,000	20,000
Opening Capitals	2,70,000	80,000

Since drawings appear in the Balance Sheet, it means that these have not been deducted from the partner's capitals so far. Hence, in order to calculate the opening capitals the drawings have not been added back.

	Mannu	*Shristhi*
	₹	₹
Interest on capitals @ 5% p.a.	13,500	4,000
Less : Interest on Drawings for 6 months @ 6% p.a.		
Mannu $= 40{,}000 \times \frac{6}{100} \times \frac{6}{12}$	1,200	
Shristhi $= 20{,}000 \times \frac{6}{100} \times \frac{6}{12}$		600
Balance (Cr.)	12,300	3,400
Net loss to the firm ₹12,300 + ₹3,400 = ₹15,700. This loss will be charged from Mannu and Shristhi in their profit sharing ratio, *i.e.*, 3 : 2 (Dr.)	9,420	6,280
Net Effect	(Cr.) 2,880	(Dr.) 2,880

Adjusting Entry :

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2022					
April 1	Shristhi's Capital A/c	Dr.		2,880	
	To Mannu's Capital A/c				2,880
	(Adjustment regarding interest on capital and drawings.)				

ILLUSTRATION 67.

From the following Balance Sheet of *A* and *B*, calculate interest on capital @ 5% p.a. payable to *A* and *B* for the year ending 31st March, 2022 :

Liabilities	₹	*Assets*	₹
A's Capital	1,00,000	Sundry Assets	1,92,000

B's Capital	80,000	Drawings : A	18,000
P & L Appropriation A/c — 2021-22	30,000		
	2,10,000		2,10,000

During the year ending 31st March, 2022, A's drawings were ₹18,000 and B's drawings ₹12,000. Profit during the year ending 31st March, 2022 was ₹58,000.

SOLUTION :

	A ₹	B ₹
Closing Capitals	1,00,000	80,000
Add : Drawings (which were previously deducted from the capital of B)	—	12,000
	1,00,000	92,000
Less : Share of Profit :		
Profit distributed ₹58,000 – ₹30,000 = ₹28,000	14,000	14,000
Opening Capitals	86,000	78,000
Interest on capital at 5% p.a.	4,300	3,900

Working Notes :

(1) Since A's drawings appear in the Balance Sheet, it means that his drawings have not been deducted from his capital so far and hence, his drawings have not been added back.

(2) Profits during the year ending 31st March, 2022 were ₹58,000 but ₹30,000 still appears in the balance sheet, therefore, only ₹28,000 were distributed between the partners.

(B) **When Separate Adjustment Entries for each error and omission are passed :** In this case, in place of a single adjustment entry, separate journal entries are passed for each error or omission. In this situation, analyticable table to find out net effect of all the adjustments is not prepared instead separate journal entries are passed for each error or omission by debiting or crediting Profit & Loss Adjustment A/c.

After passing all the adjustment entries, Profit and Loss Adjustment A/c is closed by debiting or crediting the Partner's Capital/Current Accounts.

ILLUSTRATION 68.

The Capital Accounts of Amar and Harsh stood at ₹2,00,000 and ₹3,00,000 respectively after the necessary adjustments in respect of drawings and net profit for the year ended 31st march 2017. It was subsequently ascertained that interest on capital @ 12% per annum was not taken into account while arriving at the divisible profits for the year.

During the year 2016-17, Amar had withdrawn ₹20,000 and Harsh's drawings were ₹10,000.

The net profit for the year amounted to ₹1,50,000.

The partners shared profits and losses in the ratio of 3 : 2.

You are required to pass the necessary journal entries to rectify the error in accounting. *(I.S.C. 2018)*

SOLUTION : JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2017					
April 1	Amar's Capital A/c	Dr.		90,000	
	Harsh's Capital A/c	Dr.		60,000	
	To Profit & Loss Adjustment A/c				1,50,000
	(Profits wrongly distributed now reversed)				
,,	Interest on Capital A/c	Dr.		45,600	
	To Amar's Capital A/c				15,600
	To Harsh's Capital A/c				30,000
	(Interest on capital provided)				
,,	Profit & Loss Adjustment A/c	Dr.		45,600	
	To Interest on Capital A/c				45,600
	(Interest on Capital transferred to P & L Adjustment A/c)				
,,	Profit & Loss Adjustment A/c	Dr.		1,04,400	
	To Amar's Capital A/c				62,640
	To Harsh's Capital A/c				41,760
	(Rectified profit credited to Partner's Capital A/cs)				

Working Note :

(1) Calculation of Opening Capital :

Particulars	Amar	Harsh
	₹	₹
Closing Capitals	2,00,000	3,00,000
Add : Drawings	20,000	10,000
	2,20,000	3,10,000
Less : Profits (₹1,50,000 in 3 : 2)	90,000	60,000
Opening Capitals	1,30,000	2,50,000
Interest on Capital @ 12%	15,600	30,000
Profit to be credited (₹1,50,000 – ₹45,600) = ₹1,04,400	62,640	41,760

ILLUSTRATION 69.

The capital accounts of Asif and Benny stood at ₹30,000 and ₹40,000 respectively after the necessary adjustments in respect of drawings and net profit for the year ended 31st March, 2016. It was subsequently ascertained that interest on capital @10% per annum and interest on drawings @5% per annum were not taken into account in arriving at the divisible profits for the year.

The drawings of the partners had been : Asif ₹1,200 drawn at the end of each half year and Benny ₹1,200 drawn at the end of each quarter.

The net profit for the year amounted to ₹20,000. The partners share profits and losses in the ratio of 3 : 2.

You are required to :

(*i*) Pass the necessary journal entries to rectify the lapse in accounting.

(*ii*) Prepare the adjusted capital accounts of the partners.

(ISC Sample Paper, 2017)

SOLUTION :

Since interest on capitals is always calculated on opening capitals and the same have not been given, first of all, it is necessary to calculate the opening capitals :

Particulars	*Asif*	*Benny*
	₹	₹
Closing Capitals as on 31st March, 2016	30,000	40,000
Less : Share of Profit (Which has already been added) 20,000 shared in the ratio of 3 : 2	12,000	8,000
	18,000	32,000
Add : Drawings (Which were previously deducted)	2,400	4,800
Opening Capitals as on 1st April, 2015	20,400	36,800

Interest on Capital :

			₹
Asif :	10% on ₹20,400	=	2,040
Benny :	10% on ₹36,800	=	3,680
Total Interest on Capital			5,720

Interest on Drawings :

			₹
Asif :	On ₹1,200 drawn on 30th Sept. 2015	$= 1{,}200 \times \frac{5}{100} \times \frac{6}{12} =$	30
	On ₹1,200 drawn on 31st March 2016	=	NIL
			30

Benny : On ₹4,800 for 4.5 months $= 4{,}800 \times \frac{5}{100} \times \frac{4.5}{12} =$ 90

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Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2016 April 1	Asif's Capital A/c	Dr.		12,000	
	Benny's Capital A/c	Dr.		8,000	
	To Profit and Loss Adjustment A/c				20,000
	(Net profit wrongly credited, now debited to Capital Accounts)				
,,	Interest on Capital A/c	Dr.		5,720	
	To Asif's Capital A/c				2,040
	To Benny's Capital A/c				3,680
	(Interest on capital credited to Capital Accounts)				

,,	Profit & Loss Adjustment A/c Dr. To Interest on Capital A/c (Interest on capital transferred to P & L Adjustment A/c)	5,720	5,720
,,	Asif's Capital A/c Dr. Benny's Capital A/c Dr. To Interest on Drawings A/c (Interest on Drawings debited to Capital Accounts)	30 90	 120
,,	Interest on Drawings A/c Dr. To Profit & Loss Adjustment A/c (Interest on Drawings transferred to P & L Adjustment A/c)	120	120
,,	Profit & Loss Adjustment A/c(1) Dr. To Asif's Capital A/c To Benny's Capital A/c (Rectified profit credited to Capital Accounts in 3 : 2)	14,400	 8,640 5,760

Note (1) : Rectified Profit : ₹20,000 – ₹5,720 + ₹120 = ₹14,400.

Dr. PARTNER'S CAPITAL ACCOUNTS (Adjusted) Cr.

Date	*Particulars*	*Asif*	*Benny*	*Date*	*Particulars*	*Asif*	*Benny*
2016		₹	₹	2016		₹	₹
April 1	To Profit & Loss Adj. A/c (Net Profit wrongly distributed)	12,000	8,000	April 1	By Balance b/d	30,000	40,000
,,	To Profit & Loss Adj. A/c (Interest on Drawings)	30	90	,,	By Profit & Loss Adj. A/c (Interest on Capital)	2,040	3,680
,,	To Balance c/d	28,650	41,350	,,	By Profit & Loss Adj. A/c (Share of Corrected Profit)	8,640	5,760
		40,680	49,440			40,680	49,440

ILLUSTRATION 70.

(When Profit by a Partner is in Deficiency.)

Xen, Sam and Tim are partners in a firm. For the year ended 31st March, 2019, the profits of the firm ₹1,20,000, were distributed *equally* amongst them, without providing for the following provisions of the partnership deed :

(*a*) Sam's guarantee to the firm that the firm would earn a profit of atleast ₹1,35,000. Any shortfall in these profits would be personally met by him.

(*b*) Profits to be shared in the ratio of 2 : 2 : 1.

You are required to pass the necessary Journal entries to rectify the error in accounting.
(ISC 2020)

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019					
March 31	Xen's Capital A/c	Dr.		40,000	
	Sam's Capital A/c	Dr.		40,000	
	Tim's Capital A/c	Dr.		40,000	
	To Profit and Loss Adjustment A/c				1,20,000
	(Profit wrongly distributed, now reversed)				
	Sam's Capital A/c	Dr.		15,000	
	To Profit and Loss Adjustment A/c				15,000
	(Shortfall in profit debited to Sam's Capital A/c)				
	Profit and Loss Adjustment A/c	Dr.		1,35,000	
	To Xen's Capital A/c				54,000
	To Sam's Capital A/c				54,000
	To Tim's Capital A/c				27,000
	(Rectified profit distributed in the ratio 2 : 2 : 1)				

Guarantee of Profit to a Partner

Sometimes a partner is guaranteed that he shall get a certain minimum amount of profits of the firm. Such a guarantee may be given either by (I) any one of the partners, or (II) by all other partners in a particular ratio. When the profits of the firm are not adequate then the 'excess' paid to the guaranteed partner should be charged to the partner who has given the guarantee.

ILLUSTRATION 71.

Aman, Babita and Suresh are partners in a firm. Their profit-sharing ratio is 2 : 2 : 1. However, Suresh is guaranteed a minimum amount of ₹10,000 as share of profit every year. Any deficiency arising on that account shall be met by Babita. The profits for the two years ending 31st March, 2021 and 2022 were ₹40,000 and ₹60,000 respectively. Prepare Profit and Loss Appropriation Account for the two years.

SOLUTION : PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *For the year ending 31st March, 2021* Cr.

Particulars	₹	Particulars	₹
To Profit transferred to :		By Profit & Loss A/c	40,000
Aman's Capital A/c	16,000		

Babita's Capital A/c 16,000 *Less* : Deficiency in Suresh's Share 2,000	14,000		
Suresh's Capital A/c 8,000 *Add* : Deficiency met by Babita 2,000	10,000		
	40,000		40,000

Working Note :

Share of Profit : Aman : $40,000 \times \frac{2}{5}$ = ₹16,000

Babita : $40,000 \times \frac{2}{5}$ = ₹16,000

Suresh : $40,000 \times \frac{1}{5}$ = ₹ 8,000

The minimum guaranteed amount to Suresh is ₹10,000 whereas, his share of profit as per the profit sharing ratio works out to be ₹8,000 only. Hence, there is a shortfall of ₹ 2,000 which will be borne by Babita.

PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *For the year ending 31st March, 2022* Cr.

Particulars	₹	*Particulars*	₹
To Profit transferred to :		By Profit & Loss A/c	60,000
Aman's Capital A/c $(60,000 \times \frac{2}{5})$	24,000		
Babita's Capital A/c $(60,000 \times \frac{2}{5})$	24,000		
Suresh's Capital A/c $(60,000 \times \frac{1}{5})$	12,000		
	60,000		60,000

Note : Suresh's share is more than the guaranteed amount, hence there is no need for any adjustment.

ILLUSTRATION 72.

A, *B* and *C* are partners sharing profits in the ratio of 5 : 4 : 1. *C* is given a guarantee that his share of profits in any given year would be ₹5,000. Deficiency if any, would be borne by *A* and *B* equally. The profits for the year ended 31st March, 2022 amounted to ₹40,000. Pass necessary entries in the books of the firm.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
March 31	Profit & Loss A/c	Dr.		40,000	
	To Profit & Loss Appropriation A/c				40,000
	(Transfer of profits)				
March 31	Profit & Loss Appropriation A/c	Dr.		40,000	
	To *A*'s Capital A/c				19,500
	To *B*'s Capital A/c				15,500
	To *C*'s Capital A/c				5,000
	(Profits distributed as per working note)				

Working Note :

Share of Profit : *A* : $40{,}000 \times \frac{5}{10} = 20{,}000$

B : $40{,}000 \times \frac{4}{10} = 16{,}000$

C : $40{,}000 \times \frac{1}{10} = 4{,}000$

C's share in profits amounts to ₹4,000 whereas the minimum guaranteed amount is ₹5,000. Hence, the deficiency will be borne by *A* and *B* equally.

PROFIT & LOSS APPROPRIATION A/C

for the year ended 31st March, 2022

Dr. Cr.

Particulars		₹	Particulars	₹
To *A*'s Capital A/c	20,000		By Profit & Loss A/c (being profit)	40,000
Less : Deficiency in *C*'s share	500	19,500		
To *B*'s Capital A/c	16,000			
Less : Deficiency in *C*'s share	500	15,500		
To *C*'s Capital A/c	4,000			
Add : Deficiency met by *A*	500			
Add : Deficiency met by *B*	500	5,000		
		40,000		40,000

ILLUSTRATION 73.

Mita, Rita and Sandra were partners in a firm, sharing profits and losses in the ratio of 2 : 2 : 1. Mita had personally guaranteed that in any year Sandra's share of profit, after allowing interest on capital to all the partners @5% per annum and charging interest on drawings @4% per annum, would not be less than ₹10,000.

The capitals of the partners on 1st April, 2015 were :

Mita ₹80,000, Rita ₹50,000 and Sandra ₹30,000.

The net profit for the year ended 31st March, 2016, before allowing or charging any interest amounted to ₹40,000.

Mita had withdrawn ₹4,000 on 1st April, 2015, while Sandra withdrew ₹5,000 during the year.

You are required to prepare the Profit and Loss Appropriation Account for the year 2015-16. *(I.S.C. 2017)*

SOLUTION : PROFIT AND LOSS APPROPRIATION ACCOUNT

for the year ended on 31st March, 2016

Dr. Cr.

Particulars		₹	*Particulars*		₹
To Interest on Capital :			By P & L A/c		40,000
Mita's Capital	4,000		By Interest on Drawings :		
Rita's Capital	2,500		Mita's Capital A/c	160	
Sandra's Capital	1,500	8,000	Sandra Capital A/c		
To Profit transferred to :			(for six months)	100	260
Mita's Capital	12,904				
Less : Transferred to					
Sandra	3,548	9,356			
Rita's Capital		12,904			
Sandra's Capital	6,452				
Add : Transferred					
from Mita	3,548	10,000			
		40,260			40,260

Working Note :

Net Profit after interest on Capitals and interest on Drawings :

40,000 + 260 – 8,000 = ₹32,260

Mita's Share	=	2/5 of 32,260	=	₹12,904
Rita's Share	=	2/5 of 32,260	=	₹12,904
Sandra's Share	=	1/5 of 32,260	=	₹ 6,452

Since Sandra's guaranteed share is ₹10,000, deficiency of ₹3,548 (*i.e.* 10,000 – 6,452) will be borne by Mita.

ILLUSTRATION 74.

Moli, Bhola and Raj were partners in a firm sharing profits and losses in the ratio of 3 : 3 : 4. Their partnership deed provided for the following :

(*i*) Interest on capital @5% p.a.

(*ii*) Interest on drawing @12% p.a.

(*iii*) Interest on partners' loan @6% p.a.

(*iv*) Moli was allowed an annual salary of ₹4,000; Bhola was allowed a commission of 10% of net profit as shown by Profit and Loss Account and Raj was guaranteed a profit of ₹1,50,000 after making all the adjustments as provided in the partnership agreement.

Their fixed capitals were Moli : ₹5,00,000; Bhola : ₹8,00,000 and Raj : ₹4,00,000. On 1st April, 2016 Bhola extended a loan of ₹1,00,000 to the firm. The net

profit of the firm for the year ended 31st March, 2017 before interest on Bhola's loan was ₹3,06,000.

Prepare Profit and Loss Appropriation Account of Moli, Bhola and Raj for the year ended 31st March, 2017 and their Current Accounts assuming that Bhola withdrew ₹5,000 at the end of each month, Moli withdrew ₹10,000 at the end of each quarter and Raj withdrew ₹40,000 at the end of each half year. *(C.B.S.E. 2018)*

SOLUTION :

Dr. PROFIT AND LOSS APPROPRIATION ACCOUNT Cr.

Particulars		₹	*Particulars*		₹
To Interest on Capital A/cs :			By Profit & Loss A/c		
Moli's Current A/c	25,000		Net Profit (After Interest		
Bhola's Current A/c	40,000		on Bhola's Loan :		
Raj's Current A/c	20,000	85,000	₹3,06,000 – ₹6,000)		3,00,000
To Salary (Moli's Current A/c)		4,000	By Interest on Drawings A/cs :		
To Commission			Moli's Current A/c	1,800	
(Bhola's Current A/c)		30,000	Bhola's Current A/c	3,300	
To Profit transferred to :			Raj's Current A/c	2,400	7,500
Moli's Current A/c	56,550				
Less : Transferred to					
Raj	37,300	19,250			
Bhola's Current A/c	56,550				
Less : Transferred to					
Raj	37,300	19,250			
Raj's Current A/c	75,400				
Add : Transferred from					
Moli	37,300				
Add : Transferred from					
Bhola	37,300	1,50,000			
		3,07,500			3,07,500

Working Notes :

(1) Interest on Drawings :

Moli : $40,000 \times \frac{12}{100} \times \frac{9}{24} = ₹1,800$

Bhola : $60,000 \times \frac{12}{100} \times \frac{11}{24} = ₹3,300$

Raj : $40,000 \times \frac{12}{100} \times \frac{6}{12} = ₹2,400$

(2) Divisible Profit = 3,00,000 + 7,500 – 85,000 – 4,000 – 30,000 = ₹1,88,500

Profit Distributed in the ratio of 3 : 3 : 4

Moli = 56,550

Bhola = 56,550

Raj = 75,400

Minimum guaranteed to Raj = 1,50,000

Excess of guaranteed amount = 1,50,000 – 75,400 = 74,600

It will be borne by Moli and Bhola in the ratio of 3 : 3 *i.e.*, equally.

Hence, Moli's Share = 56,550 – 37,300 = 19,250

Bhola's Share = 56,550 – 37,300 = 19,250

Dr. CURRENT ACCOUNTS Cr.

Particulars	*Moli*	*Bhola*	*Raj*	*Particulars*	*Moli*	*Bhola*	*Raj*
	₹	₹	₹		₹	₹	₹
To Drawings A/c	40,000	60,000	80,000	By Interest on Capital	25,000	40,000	20,000
To Interest on Drawings A/c	1,800	3,300	2,400	By Salary	4,000		
To Balance c/d	6,450	25,950	87,600	By Commi-ssion		30,000	
				By P & L App. A/c	19,250	19,250	1,50,000
	48,250	89,250	1,70,000		48,250	89,250	1,70,000

ILLUSTRATION 75.

Asha and Lata are partners with Capitals of ₹5,00,000 and ₹4,00,000 respectively, on which they are entitled to interest at 10% p.a. They divide profits in the ratio of 2 : 1. They take Sudha into partnership with 1/4th share of profits and guaranteed that her share of profits will not be less than ₹2,00,000. Sudha brought ₹3,00,000 as her capital. Any excess profits received by Sudha over her 1/4th share will be borne by Asha and Lata in the ratio of 4 : 1. Profits for the year ended 31st March 2020 before allowing interest on capitals amounted to ₹7,20,000. Distribute the profits.

SOLUTION : PROFIT & LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2020* Cr.

Particulars		₹	*Particulars*	₹
To Interest on Capital A/c :			By Profit & Loss A/c (being Profit)	7,20,000
Asha	50,000			
Lata	40,000			
Sudha	30,000	1,20,000		
To Asha's Capital A/c (See Working Note) $(4,50,000 \times \frac{2}{3})$	3,00,000			
Less : Transferred to Sudha	40,000	2,60,000		
To Lata's Capital A/c $(4,50,000 \times \frac{1}{3})$	1,50,000			
Less : Transferred to Sudha	10,000	1,40,000		

To Sudha's Capital A/c					
$(6,00,000 \times \frac{1}{4})$	1,50,000				
Add : Transferred from Asha	40,000				
Add : Transferred from Lata	10,000	2,00,000			
		7,20,000			7,20,000

Working Note :

(*i*) Net Profit after Interest on Capital $= 7,20,000 - 1,20,000 =$ ₹6,00,000

Sudha's share of profit $= 6,00,000 \times \frac{1}{4} =$ ₹1,50,000

Remaining Profit $= 6,00,000 - 1,50,000 =$ ₹4,50,000

Asha's Share $= 4,50,000 \times \frac{2}{3} =$ ₹3,00,000

Lata's Share $= 4,50,000 \times \frac{1}{3} =$ ₹1,50,000

(*ii*) Since Sudha's share amounts to ₹1,50,000 whereas minimum guaranteed amount is ₹2,00,000, the deficiency of ₹50,000 will be borne by Asha and Lata in 4 : 1.

Deficiency borne by Asha $= 50,000 \times \frac{4}{5} =$ ₹40,000

Deficiency borne by Lata $= 50,000 \times \frac{1}{5} =$ ₹10,000

Accounting Treatment of Guarantee of Minimum Profit to a Partner in Case of Loss

ILLUSTRATION 76.

Ankur and Bobby were into the business of providing software solutions in India. They were sharing profits and losses in the ratio 3 : 2. They admitted Rohit for a 1/5 share in the firm. Rohit is guaranteed a minimum profit of ₹2,00,000 for the year. Any deficiency in Rohit's share is to be borne by Ankur and Bobby in the ratio 4 : 1. Losses for the year were ₹1,00,000. Pass the necessary journal entries.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Ankur's Capital A/c	Dr.		48,000	
	Bobby's Capital A/c	Dr.		32,000	
	Rohit's Capital A/c	Dr.		20,000	
	To Profit and Loss A/c				1,00,000
	(Loss of ₹1,00,000 divided among the partners as per Working Note *i*)				
	Ankur's Capital A/c	Dr.		1,76,000	
	Bobby's Capital A/c	Dr.		44,000	
	To Rohit's Capital A/c				2,20,000
	(Deficiency of Rohit's share of profit met by Ankur and Bobby in 4 : 1)				

Working Notes :

(*i*) Rohit's Share of Loss = $1,00,000 \times \frac{1}{5}$ = ₹20,000

Remaining Loss = ₹1,00,000 – ₹20,000 = ₹80,000

Ankur's share of Loss = $₹80,000 \times \frac{3}{5}$ = ₹48,000

Bobby's share of Loss = $₹80,000 \times \frac{2}{5}$ = ₹32,000

(*ii*) Rohit is guaranteed a minimum profit of ₹2,00,000 whereas share of loss debited to his capital account is ₹20,000. Hence, he will be credited by ₹2,20,000 borne by Ankur and Bobby in the ratio of 4 : 1.

CASE BASED MCQs — 7

Ayush, Chaman and Govind were partners since 1st April 2015, and were sharing profits in 3 : 2 : 1. However they did not prepare a partnership deed. You are required to answer the following questions for the year ending 31st March, 2022 :

(*a*) Govind introduced additional capital of ₹2,00,000 and advanced a loan of ₹1,00,000 on 1st October 2021. Interest allowed to Govind will be :

(*i*) ₹9,000 (*ii*) ₹6,000
(*iii*) ₹3,000 (*iv*) Nil

(*b*) Chaman withdrew ₹5,000 per month for his personal use at the beginning of each month. Interest on drawings will be charged for an average period of :

(*i*) 6.5 months (*ii*) 5.5 months
(*iii*) 6 months (*iv*) No Interest will be charged

(*c*) Ayush expressed his desire that his son Suyash be admitted as a partner for 1/6th share, which he will forgo in his favour. Chaman has no objection to this but Govind objects to this proposal

(*i*) Suyash can be admitted since Ayush is forgoing his share of profit in favour of Suyash and remaining partners share of profit remains unaffected.

(*ii*) Suyash can be admitted since majority partners (Ayush and Chaman) do not have any objection to his admission.

(*iii*) Suyash can be admitted even if Chaman and Govind both object to his admission.

(*iv*) Cannot be admitted since all partners should agree for admitting a new partner.

(*d*) All partners agreed that Govind is to be given a minimum profit of ₹70,000 each year. Any deficiency is to be borne by Ayush and Chaman in the ratio of 2 : 3. Losses for the year ending 31st March, 2022 were ₹1,20,000. Deficiency borne by Ayush will be :

(*i*) ₹36,000 (*ii*) ₹54,000
(*iii*) ₹28,000 (*iv*) ₹ 8,000

ILLUSTRATION 77.

Anil, Sunil and Ravinder entered into a partnership on 1st April, 2019 to share profits in the ratio of 2 : 1 : 1. It was provided in the deed that Ravinder's share of profit

will not be less than ₹70,000 per annum. The losses for the year ended 31st March, 2020 were ₹2,00,000 before allowing interest ₹8,000 on Anil's Loan which is due for the current year.

You are required to show necessary account for division of loss and also pass the necessary journal entries.

SOLUTION :

PROFIT AND LOSS ACCOUNT

for the year ending on 31st March, 2020

Dr. Particulars	₹	Particulars		₹ Cr.
To Loss before interest	2,00,000	By Net Loss transferred to :		
To Interest on Anil's Loan	8,000	Anil's Capital A/c	1,04,000	
		Sunil's Capital A/c	52,000	
		Ravinder's Capital A/c	52,000	2,08,000
	2,08,000			2,08,000

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2020					
March 31	Interest on Anil's Loan A/c	Dr.		8,000	
	To Anil's Loan A/c				8,000
	(Interest provided on Anil's Loan to the firm)				
	Profit & Loss A/c	Dr.		8,000	
	To Interest on Anil's Loan A/c				8,000
	(Interest on loan charged to Profit & Loss A/c)				
	Anil's Capital A/c	Dr.		1,04,000	
	Sunil's Capital A/c	Dr.		52,000	
	Ravinder's Capital A/c	Dr.		52,000	
	To Profit & Loss A/c				2,08,000
	(Loss of ₹2,08,000 divided among the partners in 2 : 1 : 1)				
	Anil's Capital A/c	Dr.		81,333	
	Sunil's Capital A/c	Dr.		40,667	
	To Ravinder's Capital A/c				1,22,000
	(Deficiency of Ravinder's share of profit met by Anil and Sunil in their profit sharing ratio of 2 : 1)				

Working Note :

Ravinder is guaranteed a minimum profit of ₹70,000 whereas share of loss debited to his Capital Account is ₹52,000. Hence, he will be credited by ₹1,22,000 (*i.e.,* ₹70,000 + ₹52,000) borne by Anil and Sunil in their profit sharing ratio of 2 : 1)

ILLUSTRATION 78.

Ahmad, Bheem and Daniel are partners in a firm. On 1st April, 2021 the balance in their capital accounts stood at ₹8,00,000, ₹6,00,000 and ₹4,00,000 respectively.

They shared profits in the proportion of 5 : 3 : 2 respectively. Partners are entitled to interest on capital @ 5% per annum and salary to Bheem @ ₹3,000 per month and a commission of ₹12,000 to Daniel as per the provisions of the partnership deed.

Ahmad's share of profit, excluding interest on capital, is guaranteed at not less than ₹25,000 p.a. Bheem's share of profit, including interest on capital but excluding salary, is guaranteed at not less than ₹55,000 p.a. Any deficiency arising on that account shall be met by Daniel. The profits of the firm for the year ended 31st March 2022 amounted to ₹2,16,000. Prepare 'Profit and Loss Appropriation Account' for the year ended 31st March 2022.

SOLUTION : PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2022* Cr.

Particulars		₹	*Particulars*	₹
To Interest on Capital			By Profit & Loss A/c (Net Profit)	2,16,000
Ahmad	40,000			
Bheem	30,000			
Daniel	20,000	90,000		
To Salary (to Bheem)		36,000		
To Commission (to Daniel)		12,000		
To Balance c/d		78,000		
		2,16,000		2,16,000
To Net Profit transferred to :			By Balance b/d	78,000
Ahmad's Capital A/c				
₹78,000 × 5/10		39,000		
Bheem's Capital A/c				
₹78,000 × 3/10	23,400			
Add : Transferred from				
Daniel	1,600	25,000		
Daniel's Capital A/c				
₹78,000 × 2/10	15,600			
Less : Transferred to				
Bheem	1,600	14,000		
		78,000		78,000

Working Notes :

(1) Ahmad's Share of Profit is ₹39,000. Which is more than guaranteed profit.

(2) (*i*) Bheem's Share of Profit = ₹78,000 × $\frac{3}{10}$ = ₹23,400.

(*ii*) Bheem's Share of Profit + Interest on Capital = ₹23,400 + ₹30,000 = ₹53,400

(*iii*) Guaranteed Amount = ₹55,000.

(*iv*) Deficiency to be borne by Daniel = ₹55,000 – ₹53,400 = ₹1,600

ILLUSTRATION 79.

The partnership agreement of Rohit, Ali and Sneh provides that :

1. Profits will be shared by them in the ratio of 2 : 2 : 1.

2. Interest on capital to be allowed at rate of 6% per annum.
3. Interest on drawings to be charged at the rate of 3% per annum.
4. Ali to be given a salary of ₹500 per month.
5. Ali gave guarantee to the firm that the firm would earn a net profit of at least ₹80,000 per annum and any shortfall in these profits would be personally met by him.

The capitals of the partners on 1st April, 2013 were :

Rohit — ₹1,20,000; Ali — ₹1,00,000; Sneh — ₹1,00,000

During the financial year 2013-14, all the three partners withdrew ₹1,000 each at the beginning of every month.

The net profit of the firm for the year 2013-14 was ₹70,000.

You are required to prepare for the year 2013-2014 :

(*i*) Profit and Loss Appropriation Account.

(*ii*) Partners' Capital Accounts. (*I.S.C. 2015*)

SOLUTION : PROFIT AND LOSS APPROPRIATION A/C

for the year ended 31st March, 2014

Dr. Cr.

Particulars		₹	*Particulars*		₹
To Interest on Capital :			By Profit & Loss A/c (Net Profit)		70,000
(@ 6% p.a.)			By Ali's Capital A/c		10,000
Rohit	7,200		By Interest on Drawings :		
Ali	6,000		Rohit	195	
Sneh	6,000	19,200	Ali	195	
To Salary to Ali		6,000	Sneh	195	585
To Profit transferred to :					
Rohit's Capital A/c	22,154				
Ali's Capital A/c	22,154				
Sneh's Capital A/c	11,077	55,385			
		80,585			80,585

PARTNER'S CAPITAL ACCOUNTS

Dr. Cr.

Particulars	*Rohit*	*Ali*	*Sneh*	*Particulars*	*Rohit*	*Ali*	*Sneh*
2014	₹	₹	₹	2013	₹	₹	₹
March 31				April 1			
To P & L				By Bal. b/d	1,20,000	1,00,000	1,00,000
App. A/c		10,000		2014			
To Drawings	12,000	12,000	12,000	March 31			
To Int. on				By Int. on			
Drawings	195	195	195	Capital	7,200	6,000	6,000
To Bal. c/d	1,37,159	1,11,959	1,04,882	By Salary		6,000	
				By P & L App.			
				A/c	22,154	22,154	11,077
	1,49,354	1,34,154	1,17,077		1,49,354	1,34,154	1,17,077

Working Note : (*i*) Firm's profit is ₹70,000 (*i.e.*, ₹10,000 less than the amount guaranteed by Ali). As such ₹10,000 will be debited to Ali's Capital A/c and credited to P & L App. A/c.

(*ii*) Interest on each partner's drawings : $12,000 \times \frac{3}{100} \times \frac{6.5}{12} =$ ₹195

ILLUSTRATION 80.

Rahul, Shiv and Kabir were three partners sharing profits and losses in the ratio of 3 : 2 : 3. As on 1st April, 2013, their capital account balances stood at ₹80,000, ₹70,000 and ₹20,000 (Dr.) respectively. On this date they admitted Robert into the partnership with a capital of ₹40,000. He is to have 1/5th share of the profits with a guaranteed minimum share of distributable profit of ₹30,000.

It was decided that Rahul, Shiv and Kabir would suffer any excess over 1/5th going to Robert in the ratio of 2 : 2 : 1 respectively.

The new profit sharing ratio among partners being Rahul : Shiv : Kabir : Robert = 3 : 2 : 3 : 2.

The profit of the firm for the year 2013-14 was ₹1,50,000 before the following adjustments were made :

- Interest on Capital @ 10% p.a. to be allowed to the partners.
- Interest on Drawings : Kabir : ₹2,000; Shiv : ₹4,000
- Salary to Partners : Shiv : ₹7,000; Robert : ₹10,000

You are required to :

(*i*) Prepare a Profit and Loss Appropriation Account

(*ii*) Pass the journal entry to show the guaranteed minimum profits given to Robert by the firm. *(I.S.C. Sample Question Paper, 2015)*

SOLUTION : PROFIT & LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2014* Cr.

Particulars		₹	*Particulars*		₹
To Interest on Capital			By Profit & Loss A/c		
Rahul	8,000		(being profit)		1,50,000
Shiv	7,000		By Interest on Drawings		
Robert	4,000	19,000	Kabir	2,000	
To Salary			Shiv	4,000	6,000
Shiv	7,000				
Robert	10,000	17,000			
To Balance c/d		1,20,000			
		1,56,000			1,56,000
To Net Profit transferred to :			By Balance b/d		1,20,000
Rahul's Capital A/c	36,000				
Less : Transferred					
to Robert	2,400	33,600			
Shiv's Capital A/c	24,000				
Less : Transferred					
to Robert	2,400	21,600			

Kabir's Capital A/c	36,000			
Less : Transferred to Robert	1,200	34,800		
Robert's Capital A/c	24,000			
Add : From Rahul	2,400			
From Shiv	2,400			
From Kabir	1,200	30,000		
		1,20,000		1,20,000

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2014					
March 31	Profit & Loss Appropriation A/c	Dr.		1,20,000	
	To Rahul's Capital A/c				36,000
	To Shiv's Capital A/c				24,000
	To Kabir's Capital A/c				36,000
	To Robert's Capital A/c				24,000
	(Profit distributed in the ratio of 3 : 2 : 3 : 2)				
March 31	Rahul's Capital A/c	Dr.		2,400	
	Shiv's Capital A/c	Dr.		2,400	
	Kabir's Capital A/c	Dr.		1,200	
	To Robert's Capital A/c				6,000
	(Deficiency of Robert met by Rahul, Shiv and Kabir in the ratio of 2 : 2 : 1)				

Working Note :

(1) Interest on capital is not allowed to Kabir since his capital shows a Debit Balance.

(2) Robert was guaranteed a minimum share of ₹30,000 whereas his share of profit amounts to ₹24,000. Hence, the deficiency of ₹6,000 will be borne by Rahul, Shiv and Kabir in the ratio of 2 : 2 : 1 as follows :

$$\text{Rahul} = ₹6{,}000 \times \frac{2}{5} = ₹2{,}400$$

$$\text{Shiv} = ₹6{,}000 \times \frac{2}{5} = ₹2{,}400$$

$$\text{Kabir} = ₹6{,}000 \times \frac{1}{5} = ₹1{,}200$$

ILLUSTRATION 81.

(Guarantee of Profit when partnership starts during the year)

A, *B* and *C* entered into partnership on 1st July, 2021 to share Profit and Losses in the ratio of 5 : 3 : 2. *A* personally guaranteed that *C*'s share of profit after charging interest on capital @8% per annum would not be less than 1,60,000 p.a. The capital contributed were : *A* — ₹4,00,000; *B* — ₹3,00,000 and *C* — ₹2,00,000. Profit for the year ended on 31st March, 2022 was ₹4,74,000. Prepare Profit and Loss Appropriation Account.

SOLUTION : PROFIT & LOSS APPROPRIATION ACCOUNT

for the year ended 31st March, 2022

Dr. Cr.

Particulars		₹	Particulars	₹
To Interest on Capital :			By Profit and Loss A/c (Net Profit)	4,74,000
A	24,000			
B	18,000			
C	12,000	54,000		
To Net Profit transferred to :				
A's Capital A/c :				
₹4,20,000 × $\frac{5}{10}$	2,10,000			
Less : Transferred to *C*	36,000	1,74,000		
B's Capital A/c :				
₹4,20,000 × $\frac{3}{10}$		1,26,000		
C's Capital A/c :				
₹4,20,000 × $\frac{2}{10}$	84,000			
Add : Transferred from *A*	36,000	1,20,000		
		4,74,000		4,74,000

Working Note : *C*'s share of profit is 4,20,000 × $\frac{2}{10}$ = 84,000

Guaranteed Amount (for 9 months) = 1,60,000 × $\frac{9}{12}$ = ₹1,20,000

Deficiency to be borne by *A* = ₹1,20,000 – ₹84,000 = ₹36,000.

ILLUSTRATION 82.

A, B, C and *D* are partners sharing profits and losses in the ratio of 2 : 2 : 1 : 1. Their capitals as at 1st April, 2021 were ₹5,00,000; ₹4,00,000; ₹3,00,000 and ₹3,00,000 respectively.

Partners are entitled to interest on capital @8% p.a. and *C* is to get a salary of ₹15,000 per month.

D's share of profits excluding interest on capital has been guaranteed by the firm to be not less than ₹2,00,000. *C*'s share of profits including interest on capital and salary guaranteed by *B* at a minimum of ₹4,00,000.

The profits for the year ended 31st March, 2022 were ₹12,00,000 before providing for interest on capital and salary. You are required to prepare Profit and Loss Appropriation Account.

SOLUTION : PROFIT & LOSS APPROPRIATION ACCOUNT

for the year ended 31st March, 2022

Dr. Cr.

Particulars	₹	Particulars	₹
To Interest on Capitals :		By Profit and Loss A/c	

A	40,000		— Net Profit	12,00,000
B	32,000			
C	24,000			
D	24,000	1,20,000		
To C's Salary (₹15,000 × 12)		1,80,000		
To Balance c/d		9,00,000		
		12,00,000		12,00,000
To Profit transferred to :			By Balance b/d	9,00,000
A's Capital A/c :				
(2/6 of ₹9,00,000)	3,00,000			
Less : Firm's Deficiency[1] (2/5 of ₹50,000)	20,000	2,80,000		
B's Capital A/c :				
(2/6 of ₹9,00,000)	3,00,000			
Less : Firm's Deficiency (2/5 of ₹50,000)	20,000			
C's Deficiency	56,000	2,24,000		
C's Capital A/c :				
(1/6 of ₹9,00,000)	1,50,000			
Less : Firm's Deficiency (1/5 of ₹50,000)	10,000			
Add : Recovered from *B*	56,000	1,96,000		
D's Capital A/c :				
(1/6 of ₹9,00,000)	1,50,000			
Add : Deficiency recovered from *A*, *B* and *C* (20,000 + 20,000 + 10,000)	50,000	2,00,000		
		9,00,000		9,00,000

Working Notes :

(1) **Calculation of firm's deficiency :**

		₹
D's share of profit guaranteed by the firm		2,00,000
Less : *D*'s share of profit (1/6 of ₹9,00,000)		1,50,000
Firm's deficiency borne by *A*, *B* and *C* in 2 : 2 : 1		50,000

(2) **Calculation of deficiency recovered by *C* from *B* :**

C's share of profit (1/6 of ₹9,00,000)		1,50,000
Less : *C*'s share in firm's deficiency (1/5 of ₹50,000)		10,000
		1,40,000
Add : Interest on Capital	24,000	
Salary	1,80,000	2,04,000
		3,44,000

Since guaranteed amount to *C* is ₹4,00,000, he will recover ₹56,000 (*i.e.* 4,00,000 – 3,44,000) from *B*.

Minimum Earnings Guaranteed by a Partner :

ILLUSTRATION 83.

Jay, Vijay and Karan were partners of an architect firm sharing profits in the ratio of 2 : 2 : 1. Their partnership deed provided the following :

(*i*) A monthly salary of ₹15,000 each to Jay and Vijay.

(*ii*) Karan was guaranteed a profit of ₹5,00,000 and Jay guaranteed that he will earn an annual fee of ₹2,00,000. Any deficiency arising because of guarantee to Karan will be borne by Jay and Vijay in the ratio of 3 : 2.

During the year ended 31st March, 2018 Jay earned fee of ₹1,75,000 and the profits of the firm amounted to ₹15,00,000.

Showing your workings clearly prepare Profit and Loss Appropriation Account and the Capital Accounts of Jay, Vijay and Karan for the year ended 31st March, 2018.

(C.B.S.E. 2019, M.P.)

SOLUTION : PROFIT & LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2018* Cr.

Particulars		₹	*Particulars*	₹
To Salary			By Profit & Loss A/c (Net Profit)	15,00,000
Jay's Capital A/c	1,80,000		By Jay's Capital A/c	
Vijay's Capital A/c	1,80,000	3,60,000	(Deficiency in guaranteed fees	
To Profit transferred to :			₹2,00,000 – 1,75,000)	25,000
Jay's Capital A/c	4,66,000			
Less : Guarantee to				
Karan	1,60,200	3,05,800		
Vijay's Capital A/c	4,66,000			
Less : Guarantee to				
Karan	1,06,800	3,59,200		
Karan's Capital A/c	2,33,000			
Add : From Jay	1,60,200			
From Vijay	1,06,800	5,00,000		
		15,25,000		15,25,000

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	*Jay* ₹	*Vijay* ₹	*Karan* ₹	*Particulars*	*Jay* ₹	*Vijay* ₹	*Karan* ₹
To P & L Appro. A/c	25,000	—	—	By Salary	1,80,000	1,80,000	—
To Balance c/d	4,60,800	5,39,200	5,00,000	By P & L Appro. A/c (Profit)	3,05,800	3,59,200	5,00,000
	4,85,800	5,39,200	5,00,000		4,85,800	5,39,200	5,00,000

Working Note :

Profit to be Distributed = ₹15,00,000 + ₹25,000 – ₹3,60,000 = ₹11,65,000.

Division of Profit : Jay's Share of Profit = ₹11,65,000 × 2/5 = ₹4,66,000;
Vijay's Share of Profit = ₹11,65,000 × 2/5 = ₹4,66,000;
Karan's Share of Profit = ₹11,65,000 × 1/5 = ₹2,33,000.
Karan's Deficiency = ₹5,00,000 – ₹2,33,000 = ₹2,67,000,
which will be met by Jay and Vijay in the ratio of 3 : 2

Deficiency borne by : Jay = ₹2,67,000 × 3/5 = ₹1,60,200;
Deficiency borne by Vijay = ₹2,67,000 × 2/5 = ₹1,06,800.

SHORT ANSWER QUESTIONS

Q. 1. State the 'liability of a partner' in a partnership firm.
(C.B.S.E. 2019, Delhi)

[**Ans.** Liability of partners is Unlimited and Several (*i.e.*, personal assets can be utilized to pay off the debts of the firm).]

Q. 2. What is meant by 'mutual agency' in case of partnership?
(C.B.S.E. 2019, Chennai)

[**Ans.** Mutual agency means every partner works as principal for himself as well as other partners.]

Q. 3. Does partnership firm has a separate legal entity? Give reason in support of your answer.

Ans. From legal viewpoint, Partnership firm has no separte legal entity because it is not a body corporate. Its entity is affected by the retirement, death or insolvency of its partners.

Q. 4. Six friends started a partnership business by investing ₹2,00,000 each. They decided to share profit equally. Name the terms by which they will be called individually and collectively. *(C.B.S.E. Sample Paper, 2018)*

Ans. Partners are individually called 'Partners'.Partners are collectively called 'Firm'.

Q. 5. What is meant by "Unlimited Liability of a Partner"?

Ans. The personal assets of the partner can be utilized for paying firm's debts.

Q. 6. The business of a partnership firm may be carried on by all the partners or any one of them acting for all. One of the important implication of this statement is that every partner is entitled to participate in the conduct of the affairs of its business. State the second important implication of this statement. *(C.B.S.E. 2020, Kerala)*

Ans. Second implication of this statement is that there exists a relation of mutual agency among the partners.

Q. 7. What is the maximum number of partners that a partnership firm can have? Name the Act that provides for the maximum number of partners in a partnership firm.

Ans. As per Companies Act, 2013, the maximum number of partners in a partnership firm can be 50.

Q. 8. Gupta and Sharma were partners in a firm. They wanted to admit two more members in the firm. List the categories of individual other than minors who cannot be admitted by them.

Ans. (*i*) Persons of unsound mind;

(*ii*) Persons who have been declared insolvent.

Q. 9. What is partnership deed?

Ans. Partnership deed is a written agreement containing the terms and conditions agreed by the partners.

Q. 10. How are mutual relations of partners governed in the absence of Partnership Deed?

Ans. In the absence of a 'Partnership Deed', mutual relations of partners are governed according to Partnership Act, 1932.

Q. 11. State the provisions of Indian Partnership Act regarding the payment of remuneration to a partner for the services rendered.

Ans. As per the Indian Partnership Act, in the absence of partnership deed, no remuneration is allowed to any partner for the services rendered.

Q. 12. Is a sleeping* partner liable to the acts of other partners?

Ans. Yes, sleeping partner is liable to the acts of other partners.

Q. 13. Give any two reasons in favour of keeping a Partnership Deed.

Q. 14. State four important points which must be incorporated in a Partnership Deed.

Q. 15. Mention any four provisions of the Partnership Act, in the absence of Partnership Deed.

Q. 16. In the absence of Partnership Deed what are the rules relating to :—

(*i*) Interest on Partners' capitals; (*ii*) Interest on loan given by a partner; (*iii*) Profit sharing ratio; and (*iv*) Interest on Partners' drawings. *(I.S.C. 2010)*

Q. 17. *A* and *B* are partners but they do not have any partnership agreement. How will they solve the following disputes between them?

(*i*) *A* wants that profits should be shared in the capital ratio.

(*ii*) *B* wants that he should be paid salary for devoting more time for the business of the firm.

[**Ans.** (*i*) Profits will be shared equally. (*ii*) *B* will not get the salary.]

Q. 18. State two elements of the partnership deed.

[**Ans.** Two elements of partnership deed are :

(*i*) It is a written document containing the terms and conditions agreed upon by all the partners.

(*ii*) In case of any misunderstanding or dispute among the partners it acts as an evidence in the court of law.]

Q. 19. Is it necessary to have a partnership agreement in writing?

Ans. No. It is not necessary to have a partnership agreement in written form. An

* Sleeping or Dormant partners are those who do not take part in the conduct of the business.

oral agreement is equally valid. However, in order to avoid disputes, it is preferred to have a written agreement.

Q. 20. What share of profits would a 'sleeping partner' who has contributed 75% of the Total Capital get in the absence of a deed?

Ans. Equal share of profits.

Q. 21. In the absence of any provision in the partnership deed, at what rate is a working partner entitled for remuneration?

Ans. In the absence of any provision in the partnership deed, no partner is entitled for any remuneration.

Q. 22. Do all forms of business organisations prepare a Profit and Loss Appropriation Account?

[**Ans.** No, there is no need to prepare Profit & Loss Appropriation A/c in case of sole proprietorship concerns. It is prepared in case of partnership firms and companies.]

Q. 23. Why is Profit and Loss Appropriation Account prepared by a Partnership Firm?

[**Ans.** After ascertaining the Net Profit of the firm as per Profit and Loss Account, usually the Profit and Loss Appropriation Account is prepared to show how the Net Profit is to be distributed among the partners.]

Q. 24. Name any six items which are shown in 'Profit and Loss Appropriation Account'.

Q. 25. Distinguish between a Profit and Loss Account and Profit and Loss Appropriation Account.

[**Ans.** Refer Page 1.7]

Q. 26. Distinguish between charge against profit and appropriation out of profit.

[**Ans.** Refer Page 1.7]

Q. 27. Can a partner be exempted from sharing the losses in a firm? If yes, under what circumstances?

[**Ans.** Yes, if all partners agree that one or more of them shall not bear the losses.]

Q. 28. Why is it that the Capital Account of a partner does not show a "Debit Balance" inspite of regular and consistent losses year after year?

[**Ans.** When the Capital Accounts of partners are fixed, they always show a Credit Balance. All transactions relating to loss or profit, drawings, salaries etc. are shown in their Current Accounts.]

Q. 29. If the Partners' Capital Accounts are fixed, where will you record the following items :—

(*a*) Drawings made by a partner.

(*b*) Salary payable to a partner.

(*c*) Fresh capital introduced by a partner.

(*d*) Share of Profit.

(*e*) Interest on Drawings.

[**Ans.** (*a*) Debit of Current A/c (*b*) Credit of Current A/c (*c*) Credit of Capital A/c (*d*) Credit of Current A/c (*e*) Debit of Current A/c.]

Q. 30. Mention the items that may appear on the debit side of the Capital Account of a partner when the capitals are fluctuating.

[**Ans.** (*i*) Drawings; (*ii*) Interest on Drawings; (*iii*) Share of loss; (*iv*) Loss on revaluation; (*v*) Any assets taken by partner. (*vi*) Closing Cr. balance of the Capital.]

Q. 31. Mention the items that may appear on the credit side of the capital account of a partner when the capitals are fluctuating.

[**Ans.** Opening credit balance of Capital, Additional Capital introduced, Share of profit, Interest on capital, Salary to a partner.]

Q. 32. List any two circumstances under which the fixed capital of partners may change. *(I.S.C. 2012)*

[**Ans.** Following are the circumstances under which the fixed capital of partners may change :

(*i*) Fresh capital introduced by a partner, and

(*ii*) Capital withdrawn by a partner permanently with the consent of other partners.]

Q. 33. What is the nature of Current Accounts when partners' Capital Accounts are maintained on a fixed basis?

[**Ans.** When capitals of the partners are required to be fixed, as per the agreement, then a separate Current Account is opened for each partner to record the transactions between the firm and the partners. The Current Account records entries relating to drawings, interest on Capitals, interest on drawings, salary to partner, share of profit or loss etc. The Current account is a personal account and at the end of each financial year its balance is shown on the Balance Sheet as a separate item distinct from Capital Account.]

Q. 34. How is a debit balance on a partner's Current Account dealt with? *(I.S.C. 1993)*

[**Ans.** In case a partners' Current Account shows a debit balance after all adjustments relating to interest on Capital, salary, share of profit, drawings, interest on drawings etc., it would indicate that the partner has withdrawn in excess of what was due to him. The partner may be required either to refund the debit balance shown by his Current Account or to extinguish the debit balance by reducing his subsequent drawings. While preparing Balance Sheet the debit balance of a partner's Current Account may either be shown on the liabilities side as a deduction from his fixed Capital Account to indicate the net capital retained by the partner or on the assets side below the current assets. The former option is preferred because it presents a more accurate position of the firm in comparison to the latter.]

Q. 35. Distinguish between Drawings Account and Current Account of a partner.

[**Ans.** Points of Distinction :

(*i*) The Drawing Account records only the amounts withdrawn by a partner from time to time whereas the Current Account records all entries relating to transactions between the firm and the partners such as interest on capital, salary, share of profit or loss, drawings, interest on drawings etc.

(*ii*) The Drawings Accounts may be maintained irrespective of whether the capitals are fixed or fluctuating whereas Current Accounts are maintained only in case of fixed capitals.

(*iii*) The Drawing Account will always show a debit balance whereas the Current Account may show either a debit or credit balance.

(*iv*) At the end of each financial period, Drawing Account of each partner is closed by a transfer to the debit of his Capital Account whereas the balance of Current Account is shown as a separate item in the Balance Sheet.]

Q. 36. What are the reasons for keeping separate Capital and Current Accounts for each partner?

[**Ans.** A separate Capital and Current Account for each partner is opened :

(*i*) to ensure that the Capital remains intact and is not withdrawn;

(*ii*) to facilitate the calculation of interest on Capital;

(*iii*) to facilitate the calculation of interest on Current Accounts.

(*iv*) to separately portray the effect of personal entitlements of a partner from the business and his withdrawals.]

Q. 37. Under fluctuating Capital method, why is it necessary to open a separate Drawings Account for each partner?

[**Ans.** Even where a fluctuating Capital method is adopted, it is usual to maintain separate Drawing Account for each partner. The reasons are :

(*i*) The Drawing Account records the withdrawals of a partner from time to time and thus the Capital Account is not burdened with so many entries for drawings. Only at the end of the financial period, the balance of Drawing Account is transferred to Capital Account.

(*ii*) The Drawing Account separately shows the total drawings of a partner during a financial period.]

Q. 38. What is the adjustment and closing entry required at the time of finalisation of accounts for interest on Capital allowed to partners assuming that accounts are maintained under fixed capital system? *(I.S.C. 2017)*

[**Ans.** (*i*) Adjusting Entry :

Interest on Capital A/c ... Dr.

To Partner's Current A/c

(Interest on Capital at .....% p.a.)

(*ii*) Closing Entry :

Profit and Loss Appropriation A/c ... Dr.

To Interest on Capital A/c

(Transfer of interest on Capital)

Q. 39. In what way would you deal with rent paid to a partner for the use of his premises by the firm in which he is a partner and why? *(I.S.C. 1999)*

[**Ans.** Rent paid to a partner will be dealt with in the same manner as rent paid to an outsider. It is an usual business expense and will be debited to Profit and Loss Account. It will not be taken to Profit and Loss Appropriation Account because it is not an appropriation of profit and it is not the duty of a partner to provide premises for the business.]

Q. 40. What is interest on Capital? Give one reason why it is allowed to partners. *(I.S.C. 2002)*

[**Ans.** Interest on Capital is the apportionment of a part of profit in Capital ratio. The idea for providing the interest on Capital is to compensate those partners who contribute Capital in excess of what is required as per their profit sharing ratio.]

Q. 41. Give one reason why partners are charged interest on drawings. *(I.S.C. 2003)*

[**Ans.** Interest on drawings is charged to compensate the partners with less drawings because interest credited to Profit & Loss Appropriation Account will be distributed in profit sharing ratio.]

Q. 42. Distinguish between drawings against profit and drawings against capital. *(I.S.C. 2002)*

[**Ans.** Drawings against profit means drawings made out of resources generated by the day-to-day business activities. Such drawings do not reduce the Capital of the firm.

Drawings against Capital means drawings made in excess of profits. Such drawings reduce the Capital of the firm since they have been made in excess of resources generated by business activities.]

Q. 43. Mention two points of difference between the legal provisions regarding interest on loan and interest on drawings.

Q. 44. How is interest on drawings calculated? Give names of the methods.

Q. 45. How will you calculate interest on the drawings of equal amounts on the first day of every month of a calendar year?

Q. 46. How will you calculate interest on the drawings of equal amounts on the last day of every month of a calendar year?

Q. 47. *A* has invested ₹1,00,000 and *B* ₹25,000 and they earned a profit of ₹15,000. How much profit *A* and *B* would get?

[**Ans.** ₹7,500 each.]

Q. 48. State the two situations under which interest on capital is generally provided.

[**Ans.** 1. When the partner contribute unequal amounts of capital but share profits equally.

2. When Capital contribution is same but the share of profits are unequal.]

Q. 49. In the absence of provision in the partnership deed, in which ratio is the deficiency arising out of guarantee of profits to a partner borne by the other partners?

[**Ans.** In their old profit sharing ratio.]

Q. 50. *A* and *B* are partners in a firm. State by giving reasons whether their claims are valid if partnership deed is silent in the following matters :—

(*i*) *B* had advanced a loan to the firm. He claims interest at the usual interest rate charged by banks. The rate of interest is 12% p.a.

(ISC Specimen Question Paper, 2018)

(*ii*) *A* has contributed ₹1,00,000 and *B* ₹50,000 as capital. *B* wants profits to be shared equally.

[**Ans.** (*i*) *B* will be given interest on his loan @ 6% per annum.

(*ii*) In the absence of any agreement to the contrary, profits will be shared equally, irrespective of their capitals.]

Q. 51. *X* and *Y* are partners in a firm. They do not have any partnership deed. What should be done in the following cases :—

(*a*) *X* has invested ₹1,00,000 and *Y* only ₹50,000 as capital. *X* wants interest on capital @ 12% p.a.

(*b*) *X* spends twice the time that *Y* devotes to the business. He wants a salary of ₹2,000 per month for the extra time spent by him.

(*c*) *X* wants to introduce his son Rajesh into the business. *Y* objects it.

(*d*) *X* has given a loan of ₹20,000 to the firm. He wants interest on it @ 8% p.a.

[**Ans.** (*a*) No interest on capital will be allowed. (*b*) *X* is not entitled to any salary.

(*c*) *X*'s son cannot be admitted as a partner, if *Y* objects it. (*d*) *X* is entitled to claim interest on his loan @ 6% p.a.]

Q. 52. The following differences have arisen among *A*, *B* and *C*. Give your decision regarding the same :—

(*a*) *A* used ₹1,00,000 belonging to the firm and made a profit of ₹75,000 in speculation. *B* and *C* want that *A* should return ₹1,75,000 to the firm, while *A* wants to return ₹1,00,000 only.

(*b*) *A* used ₹50,000 belonging to the firm and suffered a loss of ₹20,000 in speculation. He wants to return only ₹30,000.

(*c*) *A* and *B* want to admit Mohan as a new partner, but *C* does not agree.

(*d*) *A* and *B* want to purchase goods from Raghubir for the firm but *C* does not agree.

[**Ans.** (*a*) *A* must return ₹1,75,000; (*b*) *A* must return ₹50,000; (*c*) Mohan cannot be admitted; (*d*) Goods may be purchased from Raghubir.]

Q. 53. How will you settle the following disputes?

(*i*) *A* and *B* are equal partners. *A* has provided a capital of ₹5,00,000 whereas *B* has provided only ₹1,00,000 as capital. *B*, however, has advanced ₹2,00,000 as loan to the firm. What interest, if any, will be given to *A* and *B*?

(*ii*) *A* has drawn ₹50,000 from the firm for personal use. *B* and *C* demand that interest should be charged @12% per annum.

(*iii*) *C* proposed that interest on drawings should be charged. *D* opposes it.

[**Ans.** (*i*) Interest on capital will not be allowed to any partner. Hence, *A* and *B* will not get interest on their capitals. Interest on Loan is allowed @ 6% p.a. Thus, *B* will get interest on loan @6% p.a.

(*ii*) In the absence of Partnership Deed, interest will not be charged on *A*'s drawings.

(*iii*) Interest on drawings cannot be charged if not provided in the Partnership Deed.]

Q. 54. Give the provisions of the Partnership Act with respect to the Interest on Capital of the Partners.. *(I.S.C. 2006)*

[**Ans.** Refer Page 1.57]

Q. 55. State the closing entries for :

(*a*) rent paid to a partner;

(*b*) interest on loan allowed to partners. *(I.S.C. 2008)*

[**Ans.** (*a*) Profit & Loss A/c Dr.

To Rent A/c

(Closing of rent paid to the partner's A/c)

(*b*) Profit & Loss A/c Dr.

To Interest on Partner's Loan A/c

(Closing of interest on partner's loan A/c)]

Q. 56. State two differences between interest on capital allowed to partners and interest on drawings charged to partners. *(I.S.C. 2008)*

Ans.

	Interest on Capital	**Interest on Drawings**
1. Objective	It is allowed to compensate those partners who contribute capital in excess of what is required as per agreed profit sharing ratio.	It is charged to prevent one partner getting an advantage over other.
2. Recording	It is debited to Profit & Loss Appropriation A/c and credited to Partner's Capital A/c.	It is credited to Profit & Loss Approparition A/c and debited to Partner's Capital A/c.

Q. 57. The firm with *X, Y* and *Z* as partners earned a profit of ₹3,00,000 during the year ended 31st March, 2011. 20% of this profit was to be transferred to General Reserve. Pass the necessary journal entry for the same. *(I.S.C. 2012)*

Ans.

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2011				
March 31	Profit & Loss Appropriation A/c Dr.		60,000	
	To General Reserve A/c			60,000
	(20% of the profit transferred to General Reserve)			

Q. 58. What accounting steps are taken by a partnership firm when a new partner is unable to bring the business guaranteed by him? *(I.S.C. 2013)*

[**Ans.** When the new partner fails to bring the business guaranteed by him, the short-fall in profit arising therefrom will be debited to his Capital/Current Account and credited to the Profit and Loss Appropriation Account.]

Q. 59. Give two differences between fixed and fluctuating capital accounts. *(I.S.C. 2014)*

Distinction Between Fixed Capital Accounts and Fluctuating Capital Accounts :

	Basis of Distinction	Fixed Capital Accounts	Fluctuating Capital Accounts
1.	**Change in Capital**	When the Capitals are fixed, the balances in capital accounts usually remain unchanged during the life-time of business, except in extraordinary circumstances.	When the Capitals are fluctuating, the balances in Capital Accounts go on changing from time to time.
2.	**Number of Accounts**	When the Capitals are fixed, each partner has two accounts, namely, Capital Account and a Current Account.	When the Capitals are fluctuating, each partner has only one account, namely, Capital Account.

Q. 60. State the provisions of the Indian Partnership Act, 1932, regarding charging of interest on drawings from a partner when :

(*a*) The firm has a partnership deed.

(*b*) The firm does not have a partnership deed. *(I.S.C. 2014)*

[**Ans.** (*a*) When the firm has a partnership deed, interest on drawings will be charged only if it is provided in the partnership deed.

(*b*) When the firm does not have a partnership deed, interest on drawings will not be charged.]

Q. 61. Give the adjusting entry and the closing entry for recording commission allowed to a partner, when the firm follows the fixed capital method. *(I.S.C. 2015)*

[**Ans.** (*i*) Adjusting Entry :

Partner's Commission A/c Dr.

To Partner's Current A/c

(Commission allowed to the partner)

(*ii*) Closing Entry :

Profit and Loss Appropriation A/c Dr.

To Partner's Commission A/c

(Transfer of Commission)

Q. 62. State giving reason whether interest on loan given by a partner to the firm be paid if there are losses.

[**Ans.** Yes, because interest on loan is a charge against profits.]

Q. 63. State two differences between partner's loan account and partner's capital account. *(I.S.C. 2015)*

[**Ans.** (1) In the absence of an agreement, partners are not entitled to any interest on capital but a partner is entitled to interest @ 6% p.a. on any loan provided by him to the firm.

(2) Partner's Loan Account will always show a Credit Balance whereas Partner's Capital Account may reflect a debit or a credit balance if the capitals are based on fluctuating capital method.]

Q. 64. Why salary and commission paid to partners are recorded in Profit & Loss Appropriation Account instead of Profit & Loss Account?

[**Ans.** Salary and Commission paid to partners are appropriation of profits and not a charge. Hence they are debited to Profit & Loss Appropriation Account.]

Q. 65. Mention a case where Profit & Loss Appropriation Account will be prepared even if Profit & Loss Account discloses net loss.

[**Ans.** In case of Interest on Drawings.]

Q. 66. Mita and Mohan are partners sharing profits and losses in the ratio of 1 : 2 with capitals of ₹15,000 and ₹25,000 respectively. The partnership deed provides for interest on capital@ 6% per annum. The trading loss for the year ending 31st March, 2016 was ₹1,500. State, giving reason, the amount of interest on capital which will be allowed to the partners. *(I.S.C. Sample Paper, 2017)*

[**Ans.** Interest on Capital will not be allowed]

Q. 67. Mittal & Sons earned a profit of ₹2,75,000 during the year ended 31st March, 2016. 10% of this profit was to be transferred to Investment Fluctuation Reserve. Pass the necessary journal entry for the same. *(I.S.C. Sample Paper, 2017)*

Ans. JOURNAL ENTRY

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Profit and Loss Appropriation A/c	Dr.		27,500	
	To Investment Fluctuation Reserve A/c				27,500
	(10% of profit transferred to Investment Fluctuation Reserve)				

Q. 68. Give the adjusting entry and closing entry for interest on loan taken by a partner from the firm, when the firm follows the Fluctuating Capital Method. *(I.S.C. 2018)*

Ans. (*i*) **Adjusting Entry :**
Partner's Capital A/c Dr.
To Interest on Partner's Loan A/c
(Interest charged on Loan taken by the partner)

(*ii*) **Closing Entry :**
Interest on Partner's Loan A/c Dr.
To Profit & Loss A/c
(Closing of Interest on Loan taken by the partner)

Q. 69. Chhavi and Neha were partners in a firm sharing profits and losses equally. Chhavi withdrew a fixed amount of ₹6,000 at the beginning of each quarter. Interest on drawings is charged @ 6% p.a.

Pass necessary journal entry for charging interest on drawings at the end of the year. *(C.B.S.E. 2019, M.P.)*

[**Ans.** Chhavi's Capital A/c Dr. 900
To Interest on Drawings A/c 900
(Interest on drawings charged)]

Q. 70. Mention two items that may appear on the debit side of a Partner's Fixed Capital Account.

[**Ans.** (*i*) Permanent withdrawal of Capital from business, and (*ii*) Closing Balance of Capital.

Q. 71. Mention two items that may appear on the credit side of a Partner's Fixed Capital Account. *(I.S.C. 2019)*

[**Ans.** (*i*) Opening Balance of Capital, and (*ii*) Additional Capital Introduced.]

Q. 72. How will a firm deal with a situation when its partnership deep provides for interest on capital, but the profit earned by it is not enough to do so, at the rate mentioned in the deed? *(I.S.C. 2020)*

Ans. Interest will be restricted to the amount of profit. Hence, profit will be distributed in the ratio of interest on capital of each partner.

Q. 73. Anna and Bobby were partners sharing profits and losses in the ratio of 5 : 3. On 1st April, 2014, their Capital Accounts showed balances of ₹3,00,000 and ₹2,00,000 respectively. Calculate the amount of profit to be distributed between the partners if the Partnership Deed provided for Interest on Capital @10% p.a. and the firm earned a profit of ₹45,000 for the year ended 31st March, 2015.

Ans. Profit of ₹45,000 in not adequate to pay interest on capital. Hence, profit of ₹45,000 will be distributed in the ratio of interest on capital i.e. ₹30,000 : ₹20,000 or 3 : 2. Thus Anna will get ₹27,000 and Bobby will get ₹18,000.

PRACTICAL QUESTIONS

(Question Nos. 1 to 79 are strictly in the serial order of Illustrations)

Q. 1. *X* and *Y* are partners sharing profits in the ratio of 2 : 1. The undermentioned trial balance was extracted from their books as at 31st March, 2022 :

	Dr. Balances	*Cr. Balances*
	₹	₹
X's Capital		3,20,000
Y's Capital		2,40,000
X's Drawings	40,000	
Y's Drawings	32,000	
Stock (1st April, 2021)	45,200	
Purchases and Sales	8,68,000	12,45,000
Debtors and Creditors	1,52,000	48,000
Buildings	6,00,000	
Cash in Hand	5,900	
Bank Overdraft		27,500
Salaries to Staff	74,700	
Rent	26,400	
Advertising Expenditure	5,000	
Travelling Expenses	31,300	
	18,80,500	18,80,500

You are required to prepare the Profit and Loss Account and **Profit and Loss Appropriation Account** for the year ended 31st March, 2022 and a Balance Sheet as on that date. The following adjustments are to be made :

(*i*) The value of stock on March 31, 2022 was ₹64,000.

(*ii*) Charge depreciation on Buildings at 10%.

(*iii*) Provide for outstanding rent ₹2,400.

(*iv*) Partners are entitled to interest on Capital @ 5% and *X* is entitled to a salary of ₹48,000 p.a.

[**Ans.** Gross Profit ₹3,95,800; Net Profit as per Profit & Loss A/c ₹1,96,000; Profit transferred to Capital Accounts as per Profit & Loss Appropriation A/c ₹1,20,000; Capitals *X* ₹4,24,000 and *Y* ₹2,60,000; Total of Balance Sheet ₹7,61,900.]

Q. 2. Girish and Satish are partners in a firm. Their Capitals on April 1, 2019 were ₹5,60,000 and ₹4,75,000 respectively. On August 1, 2019 they decided that their Capitals should be ₹5,00,000 each. The necessary adjustment in the Capitals were made by introducing or withdrawing cash. Interest on Capital is allowed at 6% p.a. You are required to compute interest on Capital for the year ending March 31, 2020.

[**Ans.** Interest on Capitals : Girish ₹31,200 and Satish ₹29,500.]

Q. 3. *X, Y* and *Z* are partners in a firm. Their Capitals as on April 1 , 2019 were ₹5,00,000; ₹4,00,000 and ₹3,00,000 respectively. On July 1, 2019 they introduced further Capitals of ₹1,00,000; ₹80,000 and ₹50,000 respectively. On February 1, 2020 *Y* withdrew ₹15,000 from his Capital. Interest is to be allowed @ 8% p.a. on the Capitals. Compute interest on Capitals for the year ending March 31, 2020.

[**Ans.** Interest on Capitals : *X* ₹46,000; *Y* ₹36,600 and *Z* ₹27,000.]

Fluctuating Capitals

Q. 4. On 1st April, 2021, *A* and *B* commenced business with Capitals of ₹6,00,000 and ₹2,00,000 respectively. On 31st March, 2022 the net profit (before taking into account the provisions of deed) was ₹2,40,000. Interest on capitals is to be allowed at 6% p.a. *B* was entitled to a salary of ₹60,000 p.a. The drawings of the partners *A* and *B* were ₹60,000 and ₹40,000 respectively. The interest on Drawings for *A* being ₹2,000 and *B* ₹1,000. Assuming that *A* and *B* are equal partners, prepare the Profit & Loss Appropriation A/c and Partner's Capital Accounts as at 31st March, 2022.

[**Ans.** Divisible Profits ₹1,35,000; Capitals *A* ₹6,41,500 and *B* ₹2,98,500.]

Note : In the absence of information, Capitals will be treated fluctuating.

Q. 5. *X* and *Y* are partners with capitals of ₹1,00,000 and ₹80,000 respectively on 1st April, 2021 and their profit sharing ratio is 2 : 1. Interest on capital is agreed @ 12% p.a. *Y* is to be allowed an annual salary of ₹6,000. The profit for the year ending 31st March, 2022 amounted to ₹50,000. Manager is entitled to a commission of 10% of the profits.

Prepare Profit and Loss Appropriation Account and Capital Accounts.

[**Ans.** Divisible Profit ₹17,400; Commission to manager is 10% of ₹50,000, *i.e.*, ₹5,000. Balances of Capital Accounts : *X* ₹1,23,600 and *Y* ₹1,01,400.]

Q. 6. *A* and *B* are partners in a firm sharing profits or losses in the ratio of 2 : 3 with capitals of ₹4,00,000 and ₹8,00,000 respectively. Each partner is entitled to 10% p.a. interest on his capital. *B* is entitled a commission of 10% on net profit remaining after deducting interest on capital but before charging any commission. *A* is entitled a commission of 8% of net profit remaining after deducting interest on capital and after

charging all commissions. The profit for the year prior to calculation of interest on capital was ₹6,00,000.

Prepare Profit and Loss Appropriation Account.

[**Ans.** Share of Profit *A* ₹1,60,000 and *B* ₹2,40,000; Commission to *B* ₹48,000 and to *A* ₹32,000.]

Fixed Capitals

Q. 7. *Y* and *Z* are partners with capitals of ₹25,000 and ₹15,000 respectively on 1st April, 2021. Each partner is entitled to 9% p.a. interest on his capital. *Z* is entitled to a salary of ₹6,000 p.a. together with a commission of 6% of Net Profit remaining after deducting interest on capitals and salary and after charging his commission. The profits for the year ended 31st March, 2022 before making any of the above mentioned adjustments amount to ₹30,800. Prepare Partner's Capital Accounts : (*i*) When capitals are fixed, and (*ii*) when capitals are fluctuating.

[**Ans.** Divisible Profits ₹20,000.

(*i*) When capitals are fixed :

Current A/c balances : *Y* ₹12,250 (Cr.); *Z* ₹18,550 (Cr.)
Capital A/c balances : *Y* ₹25,000 (Cr.); *Z* ₹15,000 (Cr.)

(*ii*) When capitals are fluctuating :

Capital A/c balances : *Y* ₹37,250 (Cr.); *Z* ₹33,550 (Cr.)]

Hint : When the profit sharing ratio of the partners is not given in the question, the profits will be shared equally.

Q. 8. *X* and *Y* were partners in a firm sharing profits in the ratio of 2 : 1. On 1st April, 2021 their fixed capitals were ₹6,20,000 and ₹2,40,000 respectively. On 1st Nov., 2021 they decided that their total capital (fixed) should be ₹9,00,000 in their profit sharing ratio. Accordingly, they introduced extra capital or withdrew excess capital. The partnership deed provided for the following :

(*i*) A monthly salary of ₹4,000 to *X*.

(*ii*) Interest on Capital @ 9% p.a.

(*iii*) Interest on drawing @ 12% p.a.

The drawings of *X* and *Y* during the year were as follows :

	X	*Y*
	₹	₹
June 1, 2021	20,000	28,000
Nov. 30, 2021	40,000	—
Feb. 1, 2022	15,000	10,000

During the year ended 31.3.2022 the firm earned a net profit of ₹3,00,000. 20% of this profit was to be transferred to general reserve. You are required to prepare :

(*i*) Profit and Loss Appropriation Account,

(*ii*) Capital Accounts of partners, and

(*iii*) Current Accounts of partners.

[**Ans.** Divisible Profit ₹1,20,000; Capital Account balances : *X* ₹6,00,000 and *Y* ₹3,00,000; Current Account balances : *X* ₹1,04,150 and *Y* ₹22,850.]

Hint. Interest on capital *X* ₹55,050 and *Y* ₹23,850.
Interest on Drawings *X* ₹3,900 and *Y* ₹3,000.

Q. 9. *A, B* and *C* entered into partnership on 1st April 2021 with capitals of ₹10,00,000, ₹8,00,000 and ₹5,00,000 respectively. On 1st July 2021, *B* advanced ₹2,00,000 and on 1st December 2021 *C* advanced ₹1,00,000 by way of loans to the firm.

The Profit and Loss Account for the year ended 31.3.2022 disclosed a profit of ₹7,70,000 but the partners could not agree upon the rate of interest on loans and the profit sharing ratio. Prepare partner's Capital A/cs and Loan A/cs.

[**Ans.** Balance of Capital A/cs *A* ₹ 12,53,000, *B* ₹10,53,000 and *C* ₹7,53,000.]

Hint : In the absence of agreement, Interest on loan is to be paid @6% p.a. and profit will be shared equally.

Q. 10. Lata and Mamta are partners with capitals of ₹3,00,000 and ₹2,00,000 respectively sharing profits as Lata 70% and Mamta 30%. During the year ended 31st March 2022 they earned a profit of ₹2,26,440 before allowing interest on partner's loan. The terms of partnership are as follows:

(*i*) Interest on Capital is to be allowed @ 7% p.a.

(*ii*) Lata to get a salary of ₹2,500 per month.

(*iii*) Interest on Mamta's Loan account of ₹80,000 for the whole year.

(*iv*) Interest on drawings of partners at 8% per annum. Drawings being Lata ₹36,000 and Mamta ₹48,000.

(*v*) 1/10th of the distributable profit should be transferred to General Reserve.

Prepare the Profit and Loss Appropriation Account.

[**Ans.** Share of Profit : Lata ₹1,00,800 and Mamta ₹43,200.]

Hints :

(*i*) Interest on Loan will be calculated at 6% p.a.

(*ii*) Interest on Drawings will be calculated for an average period of 6 months.

(*iii*) Transfer to General Reserve will be 10% of net profit i.e. 10% of 1,60,000 = ₹16,000.

Q. 11. *A, B* and *C* are partners sharing the profits and losses in the ratio of 2 : 3 : 5. On 1st July, 2019, *A* and *B* granted loans of ₹2,00,000 and ₹1,00,000 respectively to the firm. Show the distribution of profits/losses for the year ended 31st March, 2020, in the following cases :

Case (*a*) If the profits before interest for the year amounted to ₹7,500.
(*b*) If the loss before interest for the year amounted to ₹7,500.

[**Ans.** Case (*a*) Share of Loss *A* ₹1,200; *B* ₹1,800 and *C* ₹ 3,000;
Case (*b*) Share of Loss *A* ₹4,200; *B* ₹6,300 and *C* ₹10,500;]

Q. 12. *A, B* and *C* are partners in a firm sharing profits and losses equally. On 1st April, 2021 their fixed capitals were ₹8,00,000, ₹6,00,000 and ₹6,00,000 respectively. On 1st October 2021, *A* advanced ₹1,00,000 to the firm whereas *C* took

a loan of ₹1,50,000 from the firm on the same date. It was agreed among the partners that *C* will pay interest @ 10% p.a.

Profit for the year ended 31st March, 2022 amounted to ₹4,20,000 before allowing or charging interest on loans. Pass journal entries for interest on loans and prepare Current Accounts of the partners.

[**Ans.** Divisible Profit ₹4,24,500; Current Account Balances : *A* ₹1,41,500 (Cr.); *B* ₹1,41,500 (Cr.) and *C* ₹1,34,000 (Cr.)]

Hint. Interest on *A*'s Loan will not be credited to his Current Account. It will be credited to his Loan A/c.

Q. 13. *P* and *Q* are partners sharing profits and losses in the ratio of 60 : 40. On 1st April, 2021, their capitals were : *P* — ₹5,00,000 and *Q* — ₹3,00,000. During the year ended 31st March, 2022, they earned a profit of ₹7,60,000 before taking into account any of the following terms of partnership :

(*i*) Interest on the capital is to be charged @ 8% p.a.

(*ii*) *P* will get commisson @ 3% on turnover.

(*iii*) *Q* will get a salary of ₹5,000 per month.

(*iv*) *Q* will get commission of 5% on profits after deduction of interest, salary and commission (including his own commission).

(*v*) *P* is entitled to a rent of ₹20,000 per month for the use of his premises by the firm.

Partner's drawings for the year were : *P* — ₹40,000 and *Q* — ₹30,000. Turnover for the year was ₹20,00,000. After considering the above factors, you are required to prepare the Profit and loss Appropriation Account and the Capital Accounts of the Partners.

[**Ans.** Share of Profit *P* ₹1,92,000 and *Q* ₹1,28,000. Balance of Capital A/cs *P* ₹9,92,000 and *Q* ₹4,98,000.]

Hints :

(*i*) Net Profit Credited to P & L Appropriation A/c : ₹7,60,000 – Rent ₹2,40,000 = ₹5,20,000

(*ii*) *Q*'s Commission $\frac{5}{105}$ of ₹3,36,000

(*iii*) Rent is credited to *P*'s Capital Account.

Q. 14. *X* and *Y* are partners in a firm sharing profits and losses in the ratio of 3 : 2 with capitals of ₹10,00,000 and ₹5,00,000 respectively. As per the partnership deed, they are to be allowed interest on capital @ 8% p.a. The net profit for the year ended 31st March, 2022 before providing for interest on capital amounted to ₹ 45,000. Show the distribution of profit.

[**Ans.** Interest on capital allowed to *X* ₹30,000 and *Y* ₹15,000.]

Q. 15. Akruti and Vibhuti were partners in a firm sharing profits in the ratio 2 : 1. The balances in their capital and current accounts as on 1st April, 2021 were as under:

	Akruti (₹)	*Vibhuti* (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts	60,000 (Dr.)	12,000 (Cr.)

The partnership deed provided that Akruti was to be paid a salary of ₹22,500 per quarter, whereas Vibhuti was to get a commission of 15% on net profit before charging such commission.

Interest on capital was to be allowed @ 6% p.a. whereas interest on drawings was to be charged @ 10% p.a. The drawings of Akruti were ₹40,000 drawn on 1st July 2021 and Vibhuti withdrew ₹30,000 on 1st Dec., 2021. The net profit of the firm for the year ended 31st March 2022 before making the above adjustments was ₹1,00,000.

Prepare Profit and Loss Appropriation Account and Partner's Current Accounts.

[**Ans.** Share of Profit : Akruti ₹83,200 and Vibhuti ₹20,800]

Hint : Available profit is ₹1,04,000. Since it is less than appropriations, it will be divided in the ratio of 1,08,000 : 27,000 *i.e.*, 4 : 1.

Interest on Drawings

Q. 16 (A). Mr. Ashok Gupta is a partner in a firm. He withdrew the following amounts during the year ended 31st March, 2022 :—

	₹
April, 30	8,000
June, 30	6,000
Sept., 30	5,000
Dec., 31	12,000
Jan., 31	10,000

Calculate interest on drawings @ 9% p.a. for the year ended on 31st March, 2022.

[**Ans.** Interest on Drawings ₹1,710.]

Q. 16 (B). *A* is a partner in a firm. During the year ended 31st March, 2022, *A*'s drawings were :

	₹
1st June	1,000
1st August	750
1st October	1,250
1st December	500
1st February	500

Interest on drawings is charged @ 10% per annum. Calculate interest on drawings of *A* for the year ended 31st March, 2022.

[**Ans.** Interest on Drawings ₹221.]

Q. 17 (A). Gopal is a partner in a firm. He withdrew ₹1,000 p.m. regularly on the first day of every month during the year ended 31st March, 2022 for personal expenses. If interest on drawings is charged @ 15% p.a. calculate the interest on the drawings of Gopal.

[**Ans.** Interest on Drawings ₹975.]

Q. 17 (B). *X*, *Y* and *Z* are partners in a firm. You are informed that (*i*) *X* draws ₹4,000 from the firm at the beginning of every month, (*ii*) *Y* draws ₹4,000 from the firm at the end of every month, and (*iii*) *Z* draws ₹4,000 from the firm in the middle of every month. Interest on drawings is to be charged @ 9% p.a. Calculate interest on partner's drawings.

[Ans. Interest on Drawings *X* ₹2,340; *Y* ₹1,980 and *Z* ₹2,160.]

Q. 18. Calculate the interest on drawings of Mr. Aditya @ 8% p.a. for the year ended 31st March, 2022, in each of the following alternative cases :

Case (*i*) If he withdrew ₹5,000 in the beginning of each quarter.

(*ii*) If he withdrew ₹6,000 at the end of each quarter.

(*iii*) If he withdrew ₹10,000 during the middle of each quarter.

[Ans. Case (*i*) ₹1,000; Case (*ii*) ₹720; Case (*iii*) ₹1,600.]

Q. 19. Calculate the interest on drawings of Sh. Ganesh @ 9% p.a. for the year ended 31st March, 2022, in each of the following alternative cases :

Case (*i*) If he withdrew ₹4,000 p.m. in the beginning of every month;

(*ii*) If he withdrew ₹5,000 p.m. at the end of every month.;

(*iii*) If he withdrew ₹6,000 p.m;

(*iv*) If he withdrew ₹72,000 during the year;

(*v*) If he withdrew as follows :

	₹
30th April, 2021	10,000
1st July, 2021	15,000
1st Oct., 2021	18,000
30th Nov., 2021	12,000
31st March, 2022	20,000

(*vi*) If he withdrew ₹12,000 in the beginning of each quarter;

(*vii*) If he withdrew ₹18,000 at the end of each quarter;

(*viii*) If he withdrew ₹18,000 during the middle of each quarter.

[Ans. Case (*i*) ₹2,340; Case (*ii*) ₹2,475; Case (*iii*) ₹3,240; Case (*iv*) ₹3,240; Case (*v*) ₹3,008; Case (*vi*) ₹2,700; Case (*vii*) ₹2,430; Case (*viii*) ₹3,240.]

Q. 20 (A). Gupta is a partner in a firm. He drew regularly ₹800 at the beginning of every month for the six months ending 31st March, 2022. Calculate interest on drawings at 15% p.a.

[Ans. Interest on Drawings ₹210.]

Q. 20 (B). Gupta is a partner in a firm. He drew regularly ₹800 at the end of every month for the six months ending 31st March, 2022. Calculate interest on drawings at 15% p.a.

[Ans. Interest on Drawings ₹150.]

Q. 20 (C). *A*, *B* and *C* are partners in a firm. For six months ending 31st March, 2022 :

A drew regularly ₹15,000 in the beginning of every month. *B* drew regularly ₹20,000 at the end of every month and *C* drew regularly ₹25,000 in the middle of every month.

Calculate interest on drawings @ 10% p.a. for six months ending 31st March, 2022.

[Ans. Interest on Drawings : *A* ₹2,625; *B* ₹2,500 and *C* ₹3,750.]

Q. 21 (A). *A, B* and *C* started business on 1st July, 2021. Calculate interest on drawings of Mr. *A* @ 9% p.a. for nine months ending 31st March, 2022, if he withdrew ₹10,000 p.m. in the beginning of every month.

[**Ans.** ₹3,375.]

Q. 21 (B). *A, B* and *C* started business on 1st July 2021. Calculate interest on drawings of Mr. *B* @ 9% p.a. for nine months ending 31st March, 2022, if he withdrew ₹10,000 p.m. at the end of every month.

[**Ans.** ₹2,700.]

Q. 21 (C). *A, B* and *C* started business on 1st July, 2021. Calculate interest on drawings of Mr. *C* @ 9% p.a. for nine months ending 31st March, 2022, if he withdrew ₹10,000 p.m.

[**Ans.** ₹3,038]

Q. 22. Current Account's Balances as on 1st April, 2021 were as :— Amit : ₹5,000 (Cr.), Namit : ₹2,000 (Cr.) and Ruchi : ₹1,000 (Dr.). Profit sharing ratio was 3 : 2 : 1. Amit gets a monthly salary of ₹1,500.

Amit draws ₹2,000 on the first day of each month and Namit draws ₹2,000 on the last date of each month while Ruchi draws ₹6,000 at the end of each quarter. Interest on drawings is to be charged @ 12% p.a. Profits for the year ending 31st March, 2022 before adjustments of interest on drawings and of salary were ₹74,040. Show Current Accounts.

[**Ans.** Divisible Profits ₹60,000; Current A/c Amit ₹27,440 (Cr.); Namit ₹3,320 (Dr.); Ruchi ₹16,080 (Dr.)]

Q. 23. *P, Q* and *R* were partners and the balance of their capital accounts on 1st April 2021 were ₹8,00,000 (Credit); ₹5,00,000 (Credit) and ₹20,000 (Debit) respectively. As per the terms of partnership agreement interest on capitals is to be allowed @ 10% p.a. and is to be charged on drawings @ 12% p.a.

Partners withdrew as follows :

(*i*) *P* withdrew ₹10,000 p.m. at the end of each month;

(*ii*) *Q* withdrew ₹1,20,000 out of capital on 1st January 2022;

(*iii*) *R* withdrew ₹1,20,000 during the year.

The profit for the year ended 31st March, 2022 amounted to ₹4,30,000.

You are required to prepare journal entries and partner's capital accounts.

[**Ans.** Share of Profit ₹1,05,600 each. Balance of Capital Accounts *P* ₹8,59,000 (Cr.); *Q* ₹5,32,600 (Cr.); and *R* ₹41,600 (Dr.).]

Hint : Interest on Drawings *P* ₹6,600 and *R* ₹7,200.

Q. 24. Active, Blunt and Circle started a business on 1st April, 2021 with capitals of ₹4,50,000, ₹6,00,000 and ₹3,50,000 respectively. According to partnership agreement :

(*i*) Profit earned in any year will be distributed as under :
Upto ₹2,70,000 — equally
Excess over ₹2,70,000 — one-half to Active, one-sixth to Blunt and one-third to Circle.

(*ii*) Provide interest on capital and drawing @6% p.a.

(*iii*) Circle is entitled to get a monthly salary of ₹4,000 and Blunt is entitled to get a monthly salary of ₹6,000. In addition to above, Circle and Blunt are entitled to get a commission of 5% each on net profit after taking into consideration salary, interest and all commissions.

Drawings of the partners during the year were :

— Active withdrew regularly ₹5,000 at the beginning of every month.
— Blunt withdrew regularly ₹7,000 at the end of every month.
— Circle withdrew ₹80,000 during the year.

The profit of the firm for the year ending 31st March, 2022 before charging all of the above adjustments was ₹5,93,120.

Distribute the profit among the partners and prepare partners' Current A/cs.

[**Ans.** Divisible Profit ₹3,59,800; Commission to Blunt and Circle ₹17,990 each; Current Accounts : Active ₹99,950; Blunt ₹1,44,647 and Circle ₹1,24,523.]

Hint : Commission to Blunt and Circle : ₹3,95,780 × $\frac{5}{110}$ = ₹17,990 each.

Q. 25. *A* and *B* are partners sharing profits and losses equally with capitals of ₹30,000 and ₹2,00,000 respectively. Their drawings during the year ending 31st March, 2022 are as follows :

		₹
A's drawings on	30-6-2021	20,000
	31-7-2021	10,000
	1-10-2021	10,000
	1- 3-2022	16,000

B drew ₹6,000 at the end of each month. The deed provides interest on capitals and drawings at 10% p.a.. Calculate interest on capitals and drawings.

[**Ans.** Interest on Capitals *A* ₹30,000; *B* ₹20,000, Interest on Drawings *A* ₹2,800; *B* ₹3,300.]

Q. 26. On 1st April, 2021, Precious, Noble and Perfect entered into partnership with capitals of ₹60,000; ₹50,000 and ₹30,000 respectively.

Perfect advanced ₹10,000 as loan to the partnership on 1st October, 2021. The Partnership Deed contained the following clauses :

(*i*) Interest on capitals @ 6% p.a.

(*ii*) Interest on drawings @ 6% p.a. Each drew ₹4,000 at the end of each quarter commencing from 30th June, 2021.

(*iii*) Working partners Precious and Noble to get salaries of ₹200 and ₹300 per month.

(*iv*) Interest on loan was given to Perfect @6% p.a.

(*v*) Profits and losses are to be shared in the ratio of 4 : 2 : 1 up to ₹70,000 and above ₹70,000 equally.

Net profit of the firm for the year ended 31st March, 2022 (before above adjustments) was ₹1,11,000.

Prepare Profit and Loss Appropriation Account and Personal Accounts of the Partners assuming capitals to be fixed.

[**Ans.** Share of Profit : Precious ₹49,127; Noble ₹29,127; and Perfect ₹19,126; Current Account balances : Precious ₹38,767; Noble ₹19,367 and Perfect ₹4,566.]

Hints : (1) Interest on Drawings of each partner :

	₹
On ₹4,000 for 9 months	180
On ₹4,000 for 6 months	120
On ₹4,000 for 3 months	60
On ₹4,000 for 0 month	0
	360

(2) Interest on Loan will not be credited to Current A/c.

Q. 27. Basu, Harish and Jadav are partners in a firm with capital contributions of ₹50,000, ₹40,000 and ₹30,000 respectively.

Their partnership agreement provides for the following :

(*i*) Interest on capitals to be allowed @ 10% p.a.

(*ii*) Interest on drawings to be charged @ 10% p.a.

(*iii*) Harish and Jadav are each to be paid salaries @ ₹500 per month.

(*iv*) Basu is to be paid a commission of 5% of the net profit.

(*v*) The remaining profits are to be divided as follows :
40% to Basu; 30% to Harish; 20% to Jadav and 10% carried to a Reserve Account.

The net profit for the year ended 31.12.2008 was ₹50,000. Basu withdrew ₹1,000 per month at the beginning of each month, Harish withdrew ₹1,000 per month in the middle of each month and Jadav withdrew ₹1,000 per month at the end of each month.

You are required to prepare the Profit and Loss Appropriation Account for the year ended 31.12.2008 only. *(I.S.C. 2009)*

[**Ans.** Share of Profit : Basu ₹10,120; Harish ₹7,590 and Jadav ₹5,060.]

Hint : Interest on Drawings : Basu ₹650; Harish ₹600 and Jadav ₹550.

Q. 28. *A* and *B* entered into a partnership on 1st April, 2021 with capitals of ₹8,00,000 and ₹6,00,000 respectively. The profit is to be shared in the ratio of 5 : 3 by both the partners. The partnership deed provides the following information :

(*i*) *A* is to receive rent of ₹45,000 per annum for the use of his premises by the firm.

(*ii*) Both the partners are to be allowed interest on capitals @ 11% p.a. and are to be charged interest on drawings @ 9% p.a.

(*iii*) Manager is to be allowed a commission @ 12% of the net profit after charging such commission.

During the year, *A* withdrew ₹5,000 at the end of every month, *B*'s drawings during the year were as follows :

Date	*Amount* (₹)
1st July, 2021	8,000
30th September, 2021	16,000

1st December, 2021	20,000
28th February, 2022	20,000

The profit earned by the firm for the year ended 31st March, 2022 was ₹4,36,457 (before providing for any of the above clauses).

From the above you are required to draft only the Profit and Loss Appropriation Account for the year ended 31st March, 2022.

[**Ans.** Divisible profit ₹2,00,000; Interest on Drawings *A* ₹2,475; *B* ₹2,010; Manager's Commission : 12/112 of ₹3,91,457.]

Q. 29. *A* and *B* are partners. *A* withdraws ₹4,000 at the end of every month whereas *B* withdraws ₹2,000 at the beginning of every month. Interest on Capitals and Drawings is to be charged @ 12% p.a. *A* is to be allowed an annual salary of ₹6,000 and *B* is to be allowed a salary of ₹400 per month. Profit for the year ending on 31st March, 2022 was ₹1,78,900 before charging the partnership salaries and interest. From the following additional information you are required to prepare Profit and Loss Appropriation Account, Capital Accounts and Current Accounts.

	A (₹)	*B* (₹)
Capital Accounts on 1-4-2021	5,00,000	3,00,000
Additional Capital introduced on 1-8-2021	1,00,000	1,00,000
Capital withdrawn on 1-1-2022	50,000	
Current Accounts on 1-4-2021	12,100 (Cr.)	5,800 (Dr.)
Loan Account on 1-10-2021	60,000	

[**Ans.** Interest on Drawings *A* ₹2,640 and *B* ₹1,560; Interest on capitals *A* ₹66,500 and *B* ₹44,000; Interest on Loan ₹1,800; Net Profit ₹30,000 each; Balances of Current Accounts *A* ₹63,960 (Cr.) and *B* ₹47,440 (Cr.)]

Q. 30. Swaraj, Viraj and Maharaj are equal partners, their balances in the fixed capital accounts for the year ended 31st March, 2022 were ₹1,80,000, ₹1,60,000 and ₹1,75,000 respectively.

The balances in their current accounts were as follows :

	₹
Swaraj	15,000 (Cr.)
Viraj	13,000 (Dr.)
Maharaj	10,000 (Dr.)

The details of each partner's drawings during the year 2021-22 are as follows :

Swaraj	₹600 at the end of each month.
Viraj	₹800 at the beginning of each month.
Maharaj	₹400 per month during 2021-22.

The partnership deed further provides that :

(*i*) Partners are to be allowed interest on Capital A/c balances @ 6% p.a. and that on Current A/c balances @ 5% p.a.

(*ii*) Partners are charged interest on drawings @ 5% p.a.

(*iii*) Maharaj is to be given a salary of ₹20,000 for the year.

(*iv*) Swaraj is entitled to a commission of 10% of the corrected net profit of the firm.

(v) Viraj is entitled to a commission of 10% of the corrected net profit of the firm after charging such commission.

During the year ended 31st March, 2022, the net profit of the firm was ₹2,00,000 after deducting Maharaj's salary which had been debited to Salaries A/c.

You are required to prepare the Profit and Loss Appropriation Account of the firm.

[**Ans.** Divisible Profits ₹1,28,045; Interest on Drawings : Swaraj ₹165, Viraj ₹260, Maharaj ₹120; Commission to Partners : Swaraj ₹22,000 and Viraj ₹20,000.]

Q. 31. *A*, *B* and *C* are partners and on 1st April, 2021, their Capital Accounts were ₹5,00,000, ₹3,00,000 and ₹1,50,000 respectively.

The Partnership deed includes the following information :

(*a*) *C* is entitled to a salary of ₹12,000 p.a.

(*b*) Partner's are to be allowed interest on Capitals @ 6% p.a. and are to be charged interest on drawings @ 12% p.a.

(*c*) *C* is entitled to an extra benefit of 5% of profits in excess of ₹50,000 after providing for para (*a*), (*b*) and (*c*).

(*d*) *B* is entitled to 1/4th of the profits after providing for all the amounts in para (*a*), (*b*) (*c*) and (*d*) and the balance profit will be shared by *A* and *C* in the ratio of 7 : 3.

A has withdrawn ₹6,800 on 31st May, 2021 and ₹10,000 on 1st Nov., 2021. *B* has withdrawn ₹2,000 at the end of each month whereas *C* has withdrawn ₹15,000 during the year.

The net profit for the year ended 31st March, 2022 before making above adjustments was ₹2,50,000.

Prepare Profit and Loss Appropriation Account and Partner's Capital Accounts for the year ended 31st March, 2022.

[**Ans.** Interest on Drawings *A* ₹1,180, *B* ₹1,320 and *C* ₹900; Extra benefit paid to *C* ₹6,400; Share of Profit *A* ₹99,680; *B* ₹35,600 and *C* ₹42,720. Balance of Capital Accounts : *A* ₹6,11,700; *B* ₹3,28,280 and *C* ₹2,04,220.]

Hints : (*i*) Extra benefit to *C* :

$$\frac{5}{105} \times ₹(2{,}50{,}000 + 3{,}400 - 57{,}000 - 12{,}000 - 50{,}000) = ₹6{,}400.$$

(*ii*) *B*'s share of profit : $\frac{1}{5}$th of ₹1,78,000.

Interest on Capital

Q. 32. *X* and *Y* are partners sharing the profits and losses in the ratio of 2 : 1 with capitals of ₹50,000 and ₹30,000 respectively. Show the distribution of profits in each of the following alternative cases :

(*i*) If the partnership deed is silent as to the Interest on Capital and the profits for the year are ₹9,000.

(*ii*) If the partnership deed provides for Interest on Capital @ 6% p.a. and the losses for the year are ₹6,000.

(*iii*) If the partnership deed provides for Interest on Capital @ 6% p.a. and the profits for the year are ₹9,000.

(*iv*) If the partnership deed provides for Interest on Capital @ 6% p.a. and the profits for the year are ₹3,000.

(*v*) If the partnership deed provides for Interest on Capital @ 6% p.a. even if it involves the firm in loss and the profits for the year are ₹3,000.

[**Ans.** Case (*i*) Profit *X* ₹6,000, *Y* ₹3,000; Case (*ii*) Loss *X* ₹4,000, *Y* ₹2,000; Case (*iii*) Profit *X* ₹2,800, *Y* ₹1,400; Case (*iv*) Interest on Capital *X* ₹1,875, *Y* ₹1,125; Case (*v*) Loss *X* ₹1,200, *Y* ₹600.]

Q. 33. *A* and *B* contribute ₹4,00,000 and ₹3,00,000 respectively as their capitals. They decide to allow interest on capital @ 8% p.a. Their respective share of profit is 3 : 2 and the profit for the year is ₹42,000 before allowing for interest on capitals. Show the distribution of profits (I) Where there is no agreement except for interest on capitals, and (II) Where there is a clear agreement that the interest on capitals will be allowed even if it involves the firm in loss.

[**Ans.** In first case, Interest on Capital *A* ₹24,000 and *B* ₹18,000. In second case, Loss *A* ₹8,400 and *B* ₹5,600.]

Q. 34. *P* and *Q* were partners in a firm sharing profits in 3 : 1 ratio. Their respective fixed capitals were ₹10,00,000 and ₹6,00,000. The partnership deed provided interest on capital @ 12% p.a. The partnership deed further provided that interest on capital will be allowed fully even if it will result into a loss to the firm. The net profit of the firm for the year ended 31st March, 2018 was ₹1,50,000.

Pass necessary journal entries in the books of the firm allowing interest on capital and division of profit/loss among the partners. *(C.B.S.E. 2019, Kerala)*

[**Ans.** Net Loss transferred to Current Accounts : *P* ₹31,500 and *Q* ₹10,500.]

Q. 35. Kavita and Leela are partners with capitals of ₹6,00,000 and ₹4,00,000 and sharing profits & losses in the ratio of 2 : 1. Their partnership deed provides that interest on capitals shall be provided @8% p.a. and it is to be treated as a charge against profits. Prepare relevant account to allocate the profit in the following alternative cases :

(*i*) If profit for the year is ₹1,10,000
(*ii*) If profit for the year is ₹ 35,000
(*iii*) If loss for the year is ₹ 10,000

[**Ans.**
Case (*i*) Share of Profit : Kavita ₹20,000; Leela ₹10,000
(*ii*) Share of Loss : Kavita ₹30,000; Leela ₹15,000
(*iii*) Share of Loss : Kavita ₹60,000; Leela ₹30,000]

Hint : Interest on Capital will be recorded in Profit & Loss Account since it is a charge against profits.

Q. 36. Lalan and Balan were partners in a firm sharing profits in the ratio of 3 : 2. Their fixed capitals on 1st April, 2021 were : Lalan ₹1,00,000 and Balan ₹2,00,000. They agreed to allow interest on capital @12% per annum and to charge on drawings @15% per annum. The firm earned a profit, before all above adjustments, of ₹30,000 for the year ended 31st March, 2022. The drawings of Lalan and Balan during the year were ₹3,000 and ₹5,000 respectively. Showing you calculations clearly, prepare Profit and Loss Appropriation Account of Lalan and Balan. The interest on capital will be allowed even if the firm incurs a loss.

[Ans. Net Loss transferred to Lalan's Current Account ₹3,240 and Balan's Current Account ₹2,160.]

Q. 37. On 1st April, 2019 *X, Y* and *Z* started a business in partnership. *X* contributes ₹90,000 at first but withdraws ₹30,000 at the end of six months. *Y* introduces ₹75,000 at first and increases it to ₹90,000 at the end of four months, but withdraws ₹30,000 at the end of eight months. *Z* brings in ₹75,000 at first but increases it by ₹60,000 at the end of seven months.

During the year ended 31st March, 2020, they make a net profit of ₹42,000. Show how the partners should divide this amount on the basis of effective capital employed by each partner.

[Ans. Profit sharing ratio of *X, Y* and *Z* = 3 : 3 : 4.]

Q. 38. *A* and *B* commenced business on 1st April, 2021 with capitals of ₹1,20,000 and ₹60,000 respectively. They decided to share profits in the Capital Ratio. You are required to calculate Capital Ratio on 31st March, 2022, on the basis of the following particulars :—

	Capital Introduced		*Capital Withdrawn*	
	A (₹)	*B* (₹)	*A* (₹)	*B* (₹)
1st July, 2021	—	15,000	30,000	—
1st October, 2021	30,000	—	—	15,000
1st December, 2021	—	18,000	—	—
1st January, 2022	—	24,000	6,000	—
1st February, 2022	9,000	—	—	4,500

Also calculate interest on capitals if it is @ 9% p.a.

[Ans. Capital Ratio 13,50,000 : 9,00,000 or 3 : 2; Interest on Capital *A* ₹10,125; *B* ₹6,750.]

Adjustments Before the Closing of Accounts

Q. 39. *A, B* and *C* are in partnership sharing profits and losses in the ratio of 2 : 1 : 1. Following particulars are available from their books :

	A	B	C
	₹	₹	₹
Capital Accounts 1st April, 2021	20,000	15,000	10,000
Current Accounts 1st April, 2021	1,500	2,500	(Dr.) 2,000
Drawings	6,000	4,000	4,000
Life Insurance Premium 1st October, 2021	2,000		

Life Insurance Premium of *A* has been paid by the firm and has been charged to General Expenses A/c. Partners are allowed 8% p.a. interest on their capitals and charged at 10% p.a. on their drawings. Profits for the year ending 31st March, 2022 amounted to ₹20,800 before taking into account the interest on capitals and drawings. While calculating profits, depreciation at the rate of 20% p. a. has been omitted on building of the value of ₹20,000. Prepare Profit and Loss Appropriation Account and Partners' Current Accounts for the year.

[Ans. Divisible Profits ₹16,000. Current A/cs *A* ₹2,700 (Cr.); *B* ₹3,500 (Cr.); *C* ₹1,400 (Dr.)]

[**Hints : (1)** If it is not clearly mentioned whether the balance of a Current Account is Debit or Credit, it will be presumed that its balance is Credit.

(2) Interest on Drawings will be calculated for six months.]

Adjustments in the Closed Accounts

Q. 40. After the accounts of the partnership have been drawn up and the books closed off, it is discovered that interest on capitals @ 8% p.a. as provided in the partnership agreement has been omitted to be recorded. Their capital accounts at the beginning of the year stood as follows : *A* ₹8,00,000; *B* ₹4,00,000; *C* ₹3,00,000. Their profit sharing ratio was 2 : 1 : 1. Instead of altering the Balance Sheet it is decided to pass necessary adjusting entry at the beginning of the next year.

You are required to give the necessary journal entry.

[**Ans.**	*C*'s Capital A/c	Dr.	6,000	
	To *A*'s Capital A/c			4,000
	To *B*'s Capital A/c			2,000]

Q. 41. *A, B, C* and *D* are partners sharing profits in 2 : 2 : 1 : 1. They distributed the profit for the year ending 31st March 2020, ₹9,00,000 without providing for the following :

(*i*) Salary to *A* @ 15,000 per month.

(*ii*) Salary to *B* and *D* @ ₹30,000 per quarter to each partner.

Give necessary adjusting journal entry.

[**Ans.**	*B*'s Capital A/c	Dr.	20,000	
	C's Capital A/c	Dr.	70,000	
	To *A*'s Capital A/c			40,000
	To *D*'s Capital A/c			50,000]

Q. 42. *A, B* and *C* are partners sharing profits and losses in the ratio of 1 : 2 : 3. They have omitted interest on capital @ 8% p.a. for two years ended 31st March, 2022. Their fixed capitals were ₹4,00,000, ₹6,00,000 and ₹8,00,000 respectively. Pass the necessary adjusting entry.

[**Ans.**	*C*'s Current A/c	Dr.	16,000	
	To *A* 's Current A/c			16,000]

Q. 43. *A, B* and *C* are partners sharing profits and losses in the ratio of 5 : 3 : 1. After the final accounts have been prepared, it was discovered that interest on drawings had not been taken into consideration. The interest on drawing of partners amounted to *A* ₹8,000, *B* ₹6,000 and *C* ₹4,000. Give the necessary adjusting journal entry.

[**Ans.**	*C*'s Capital A/c	Dr.	2,000	
	To *A*'s Capital A/c			2,000]

Q. 44. *A, B, C* and *D* are partners sharing profits and losses in 2 : 2 : 3 : 3 respectively. After the accounts of the year had been closed, it was found that interest on drawings @ 6% p.a. has not been taken into consideration. The drawings of the partners were : *A* ₹20,000; *B* ₹24,000; *C* ₹32,000 and *D* ₹44,000. Give the necessary adjusting entry.

[**Ans.**	*D*'s Capital A/c	Dr.	240	
	To *A*'s Capital A/c			120
	To *C*'s Capital A/c			120]

Q. 45. *A* and *B* were partners sharing profits in 2 : 1 ratio. During the year ended 31st March, 2022, *A*'s drawings were ₹50,000 per month drawn in the beginning of every month and *B*'s drawings were ₹25,000 per month drawn at the end of every month. After the preparation of final accounts, it was discovered that interest on *A*'s drawings @ 12% p.a. was not taken into consideration. Give the necessary adjusting entry on 1st April, 2022.

[**Ans.**	*A*'s Capital A/c	Dr.	13,000	
	To *B*'s Capital A/c			13,000]

Q. 46. Anil, Sunil and Sanjay have omitted interest on Capitals for two years ended on 31st March, 2022. Their fixed capitals in two years were Anil ₹8,00,000, Sunil ₹7,00,000 and Sanjay ₹3,00,000. Rate of interest on Capital is 10% p.a. Their profit Sharing ratios were in first year 4 : 3 : 2 and in second year 3 : 2 : 1.

Give necessary adjusting entry at the beginning of next year.

[**Ans.** Current A/cs of Anil & Sanjay will be debited by ₹10,000 each and Current A/c of Sunil will be Credited by ₹20,000.]

Q. 47. *P, Q* and *R* are partners sharing profits in the ratio of 2 : 1 : 1. Their capitals as on 1st April, 2021 were ₹50,000, ₹30,000 and ₹20,000 respectively. At the end of the year ending 31st March, 2022 it was found out that interest on capitals @ 12% p.a., salaries to *P*, ₹500 per month and *R* ₹1,000 per month were not adjusted from the profits. Show adjusting entry to be made in the next year for above adjustments.

[**Ans.** Capital A/cs of *P* and *Q* will be debited by ₹3,000 and ₹3,900 respectively; and Capital A/c of *R* will be credited by ₹6,900.]

Q. 48 (A). On 1st April, 2021 the Capitals of *A* and *B* were ₹4,00,000 and ₹2,00,000 respectively. They divided profits in their capital ratio. Profits for the year ended 31st March, 2022 were ₹3,00,000 which have been duly distributed among the partners, but the following transactions were not passed through the books :—

(*a*) Interest on Capitals @ 12% p.a.
(*b*) Interest on Drawings *A* ₹12,000; *B* ₹10,000.
(*c*) Commission due to *B* ₹20,000 on a special transaction.
(*d*) *A* is to be paid a salary of ₹50,000.

You are required to pass a journal entry on 10th April, 2022 which will not affect the P & L A/c of the firm and at the same time will rectify the errors.

[**Ans.**	*B*'s Capital A/c	Dr.	6,000	
	To *A*'s Capital A/c			6,000]

Q. 48 (B). Kumar and Raja were partners in a firm sharing profits in the ratio of 7 : 3. Their fixed capitals were : Kumar ₹9,00,000 and Raja ₹4,00,000. The partnership deed provided for the following but the profit for the year was distributed without providing for :

(*i*) Interest on capital @ 9% per annum.

(*ii*) Kumar's salary ₹50,000 per year and Raja's salary ₹3,000 per month.

The profit for the year ended 31.3.2022 was ₹2,78,000.

Pass the adjustment entry.

[**Ans.**	Kumar's Current A/c	Dr.	11,100	
	To Raja's Current A/c			11,100]

Q. 49. *A*, *B* and *C* are partners sharing profits in the ratio of 2 : 2 : 1. Their fixed capitals were ₹4,00,000, ₹2,50,000 and ₹1,00,000 respectively. Net profit for the year ending 31st March, 2022 amounted to ₹2,20,000 which was distributed without providing for the following :

(*i*) Salary to *B* ₹5,000 p.m. and to *C* ₹10,000 per quarter.

(*ii*) Interest on capital @6% p.a.

(*iii*) Commission to Manager @10% after charging such commission.

Pass necessary rectifying entry.

[**Ans.**	*A*'s Current A/c	Dr.	42,000	
	To *B*'s Current A/c			9,000
	To *C*'s Current A/c			13,000
	To Manager's Commission Outstanding A/c			20,000]

Q. 50. Suresh and Ramesh were partners in a firm sharing profits in the ratio of 3 : 2. Their fixed capitals were : Suresh ₹9,00,000 and Ramesh ₹6,00,000. The partnership deed provided for the following :

(*i*) Interest on capital @ 5% per annum.

(*ii*) ₹60,000 per annum salary to Suresh and salary ₹2,000 per month to Ramesh. The profit earned by the firm for the year ended 31-3-2022 was ₹2,34,000.

The profits were divided equally without providing for the above.

Pass adjustment entry

[**Ans.**	Ramesh's Current A/c	Dr.	33,000	
	To Suresh's Current A/c			33,000]

Q. 51. *A*, *B* and *C* were partners in a firm. On 1-4-2021 their capitals stood at ₹5,00,000, ₹2,50,000 and ₹2,50,000 respectively. As per the provisions of the partnership deed :

(*a*) *C* was entitled for a salary of ₹10,000 p.m.

(*b*) Partners were entitled to interest on capital at 5% p.a.

(*c*) Profits were to be shared in the ratios of capitals.

The net profit for the year ended 31.3.2022 of ₹3,30,000 was divided equally without providing for the above terms.

Pass an adjustment entry to rectify the above error.

[**Ans.**			₹	₹
	A's Capital A/c	Dr.	5,000	
	B's Capital A/c	Dr.	57,500	
	To *C*'s Capital A/c			62,500]

Q. 52. *A*, *B* and *C* were partners in a firm. Their capitals were *A* ₹1,00,000, *B* ₹2,00,000 and *C* ₹3,00,000 respectively on 1st April, 2021. According to the partnership deed they were entitled to an interest on capital @ 5% p.a. In addition *A* was also entitled to draw a salary of ₹5,000 per month. *C* was entitled to a commission of 5% on the profits after charging the interest on capital but before charging the salary payable to *A*. The net profits for the year ended 31st March, 2022 were ₹3,60,000 distributed in the ratio of their capitals without providing for any of the above adjustments. The profits were to be shared in the ratio 2 : 3 : 5. Pass the necessary adjustment entry showing the workings clearly.

[**Ans.**	*B*'s Capital A/c	Dr.	33,950	
	C's Capital A/c	Dr.	21,750	
	To *A*'s Capital A/c			55,700]

Q. 53. The partners of a firm distributed the profits for the year ended 31st March, 2022, ₹1,50,000 in the ratio of 2 : 2 : 1 without providing for the following adjustments:

(*i*) *A* and *B* were entitled to a salary of ₹1,500 per quarter.

(*ii*) *C* was entitled to a commission of ₹18,000.

(*iii*) *A* and *C* had guaranteed a minimum profit of ₹50,000 p.a. to *B*.

(*iv*) Profits were to be shared in the ratio of 3 : 3 : 2.

Pass necessary journal entry for the above adjustments in the books of the firm.

[**Ans.**	*A*'s Capital A/c	Dr.	12,000	
	B's Capital A/c	Dr.	4,000	
	To *C*'s Capital A/c			16,000]

Q. 54. *A*, *B* and *C* were partners in a firm. Their partnership deed provided that the profits shall be divided as follows :

First ₹60,000 in the ratio of 3 : 2 : 1;

Remaining profits will be shared equally.

The profits for the year ended 31st March, 2019 were ₹1,50,000 which had been distributed among the partners. On 1st April, 2018 their Capitals were *A* ₹4,00,000, *B* ₹3,00,000 and *C* ₹2,00,000. Interest on Capital was to be provided @ 8% p.a. which was omitted to be provided before distribution of profits.

Pass necessary rectifying entry for the same.

[**Ans.**	*C*'s Capital A/c	Dr.	8,000	
	To *A*'s Capital A/c			8,000]

Q. 55. *X*, *Y* and *Z* are partners in a firm sharing profits and losses in the ratio 5 : 3 : 2. Their capitals (fixed) are ₹2,00,000; ₹1,50,000; ₹1,25,000 respectively. For the year ended 31st March, 2022 interest on capital was credited to them @ 8% instead of 10%.

Give adjusting journal entry.

[**Ans.** *X*'s Current A/c will be debited by ₹750; *Y* and *Z*'s Current A/cs will be credited by ₹150 and ₹600 respectively.]

Q. 56. *A, B* and *C* are partners in a firm sharing profits and losses in the ratio of 4 : 3 : 3. Their fixed capitals were ₹1,00,000, ₹2,00,000 and ₹3,00,000 respectively. For the year ended 31st March, 2022 interest on capital was credited to them @ 10% instead of 9% p.a. Pass the necessary adjusting journal entry.

[**Ans.**	*B*'s Current A/c	Dr.	200	
	C's Current A/c	Dr.	1,200	
	To *A*'s Current A/c			1,400]

Note : Since the capitals are fixed, Current Accounts will be debited or credited.

Q. 57. *A, B* and *C* were partners sharing profits in the ratio of 1 : 2 : 3. *A* withdrew ₹5,000 every month, *B* withdrew ₹60,000 during the year and *C* withdrew ₹15,000 during each quarter. It was discovered that for the year ending 31st March 2021, interest on drawings was charged @ 8% p.a. whereas there is no provision for interest on drawings in the partnership deed. Pass necessary rectifying entry.

[**Ans.**	*C*'s Capital A/c	Dr.	1,200	
	To *A*'s Capital A/c			1,200]

Hint : Interest on each partner's drawings ₹2,400.

Q. 58. After the accounts of a partnership have been drawn up and the books closed off, it is discovered that for the years ended 31st March, 2021 and 2022, interest has been credited to the partners upon their capitals at 5% per annum although, no provision for interest is made in the partnership agreement.

The amounts involved are :—

	Interest Credited		
Year	*A*	*B*	*C*
	₹	₹	₹
2021	4,200	2,400	1,320
2022	4,320	2,520	1,320

You are required to put through adjusting entry as on 1st April, 2022, if the profits were shared as follows in 2021, 2 : 2 : 1 and in 2022, 3 : 4 : 3.

[**Ans.**	*A*'s Capital A/c	Dr.	2,904	
	To *B*'s Capital A/c			1,512
	To *C*'s Capital A/c			1,392]

Q. 59. Sachin, Kapil and Rashmi have been sharing profits in the ratio of 3 : 2 : 1 respectively. Rashmi wants that she should share profits equally along with Sachin and Kapil and she further wants that change in profit sharing ratio should be applicable retrospectively for the last three years. Other partners have no objection to this. The profits for the last three years were ₹60,000, ₹47,000 and ₹55,000. Record the adjustment by means of a journal entry.

[**Ans.**	Sachin's Capital A/c	Dr.	27,000	
	To Rashmi's Capital A/c			27,000]

Q. 60 (A). Mohan, Vijay and Anil are partners, their capitals being ₹30,000, ₹25,000 and ₹20,000 respectively. In arriving at these figures, the profits for the year ended, 31st March, 2022 ₹24,000 has already been credited to the partners in the proportion in which they share profits. Their drawings were ₹5,000 (Mohan); ₹4,000

(Vijay) and ₹3,000 (Anil) for the year ending 31st March, 2022. Subsequently the following omissions were noticed and it was decided to bring them into Account.

(*i*) Interest on Capital at 10% p.a.
(*ii*) Interest on Drawings Mohan ₹250, Vijay ₹200 and Anil ₹150.

Make the necessary journal entry and prepare Capital Accounts of Partners'.

[**Ans.** Opening Capitals — Mohan ₹27,000, Vijay ₹21,000, Anil ₹15,000; Dr. Anil's Capital by ₹550 and Cr. Mohan's Capital by ₹550. Adjusted Capital accounts balances Mohan ₹30,550; Vijay ₹25,000; Anil ₹19,450.]

Q. 60 (B). The capitals of *A*, *B* and *C* stood at ₹20,000, ₹15,000 and ₹10,000 respectively after the necessary adjustment in respect of drawings and net profits. Subsequently, it was discovered that interest on capital at 10% p.a. and interest on drawings ₹130, ₹90 and ₹50 respectively have been ignored. Profit of the year already adjusted was ₹10,000. Drawings of the partners were ₹1,000, ₹800 and ₹500 respectively. They share profits and losses in the ratio of 2 : 1 : 1. Give necessary journal entry to rectify the accounts.

[**Ans.** Opening Capitals : *A* ₹16,000; *B* ₹13,300 and *C* ₹8,000; Debit *A*'s Capital A/c by ₹260 and *C*'s Capital A/c by ₹115 and Credit *B*'s Capital A/c by ₹375.]

Q. 60 (C). *A* and *B* are partners in a business sharing profits and losses in the ratio of 3 : 2. Their capitals on 31st March, 2022, after the adjustment of net profits and drawings amounted to ₹2,00,000 and ₹1,50,000 respectively. Later on, it was discovered that interest on Capital at 8% per annum, as provided for in the partnership deed, had not been credited to the partners' capital accounts before the distribution of profits. The year's net profit amounted to ₹75,000 and the partners had withdrawn ₹24,000 each. Instead of altering the signed balance sheet, it was decided to make an adjustment entry at the beginning of the new year crediting or debiting the Partners' Accounts. Give the necessary journal entry as also a statement of details arriving at the amount of adjusting entry.

[**Ans.** Opening Capitals *A* ₹1,79,000 and *B* ₹1,44,000; Debit *A*'s Capital A/c by ₹1,184 and Credit *B*'s Capital A/c by ₹1,184.]

Q. 61. Assuming the capitals are fixed in Question 60 (A), (B) and (C), give the necessary adjusting journal entry.

[**Ans.**			₹	₹
(A)	Anil's Current A/c	Dr.	450	
	To Mohan's Current A/c			450
(B)	*A*'s Current A/c	Dr.	245	
	C's Current A/c	Dr.	108	
	To *B*'s Current A/c			353
(C)	*A*'s Current A/c	Dr.	800	
	To *B*'s Current A/c			800]

Q. 62. On 31st March, 2022, the balances in the capital accounts of Esha, Manav and Daman after making adjustments for profits and drawings were ₹3,20,000, ₹2,40,000 and ₹1,60,000 respectively. Subsequently, it was discovered that the interest on capital and drawings had been omitted.

- The profit for the year ended on 31st March, 2022 was ₹90,000.
- During the year, Esha and Manav each withdrew a sum of ₹48,000 in equal instalments in the middle of every month and Daman withdrew ₹60,000.
- The interest on drawings was to be charged @5% per annum and interest on capital was to be allowed @10% per annum.
- The profit-sharing ratio of the partners was 3 : 2 : 1.

Showing your workings clearly, pass the necessary rectifying entry.

[**Ans.** Opening Capitals : Esha ₹3,23,000; Manav ₹2,58,000 and Daman ₹2,05,000; Debit Esha's Capital A/c by ₹6,250 and Manav's Capital A/c by ₹300 and Credit Daman's Capital A/c by ₹6,550.]

Q. 63. The capital accounts of *A*, *B* and *C* showed credit balances of ₹5,00,000, ₹3,00,000 and ₹2,00,000 respectively, after taking into account drawings and net profit of ₹3,00,000. They shared profits in the ratio of 2 : 1 : 1. The drawings of the partners during the year 2020-21 were :

(*i*) *A* withdrew ₹10,000 at the beginning of each half year.

(*ii*) *B* withdrew ₹10,000 at the end of each half year.

(*iii*) *C*'s Drawings were :

	₹
1st May, 2020	6,000
1st October, 2020	5,000
31st Dec. 2020	4,000
31st March, 2021	5,000

Calculate interest on partners' capitals @ 8% p.a. and interest on partners' drawings @ 10% p.a. for the year ended 31st March, 2021.

[**Ans.** Interest on Capitals *A* ₹29,600; *B* ₹19,600 and *C* ₹11,600.
Interest on Drawings *A* ₹1,500; *B* ₹500 and *C* ₹900.]

Q. 64. *A* and *B* are partners in a firm sharing profits and losses in the ratio of 2 : 1. The following was the Balance Sheet of the firm as at 31.3.2022.

Liabilities		₹	*Assets*	₹
Capitals :	*A*	6,00,000	Sundry Assets	10,00,000
	B	4,00,000		
		10,00,000		10,00,000

The profits ₹4,50,000 for the year ended 31.3.2022 were divided between the partners without allowing interest on capital @9% p.a. and without charging interest on drawings @12% p.a. During the year *A* withdrew ₹1,00,000 and *B* ₹50,000.

Pass the necessary adjustment journal entry and show your working clearly.

[**Ans.** *A*'s Capital A/c	Dr.	6,000	
To *B*'s Capital A/c			6,000]

Hint : Interest on drawings will be charged for 6 months.

Q. 65. *A* and *B* are partners in a firm sharing profits and losses in the ratio of 2 : 3. The following was the Balance Sheet of the firm as at 31.3.2022.

Liabilities			₹	*Assets*	₹
Capitals :	*A*	4,90,000		Sundry Assets	7,90,000
	B	3,00,000	7,90,000		
			7,90,000		7,90,000

Profits ₹2,00,000 for the year ended 31.3.2022 were divided between the partners without allowing interest on capital @6% p.a., interest on drawings @10% p.a. and salary to *B* @ ₹5,000 per month. During the year *A* withdrew ₹40,000 and *B* withdrew ₹20,000.

Showing your working notes clearly, pass the necessary rectifying entry.

[**Ans.** *A*'s Capital A/c Dr. 13,400
To *B*'s Capital A/c 13,400]

Q. 66. *A* and *B* are partners sharing profits and losses in the ratio of 3 : 1. Following is the Balance Sheet of the firm as at 31st March, 2022.

Liabilities	₹	*Assets*		₹
A's Capital	90,000	Drawings :		
B's Capital	30,000	*A*	12,000	
		B	6,000	18,000
		Sundry Assets		1,02,000
	1,20,000			1,20,000

Profit for the year ended 31st March, 2022 ₹24,000 was divided between the partners in their profit sharing ratio, but interest on capital at 5% p.a. and on drawings at 6% p.a. was inadvertently ignored. Give the necessary adjustment entry for the adjustment of interest. Interest on drawings may be calculated on an average basis for 6 months.

[**Ans.** *B*'s Capital A/c Dr. 45
To *A*'s Capital A/c 45]

Q. 67. From the following Balance Sheet of *A* and *B*, calculate interest on capital at 5% p.a. for the year ending 31st March, 2022 :

BALANCE SHEET *as at 31st March, 2022*

Liabilities	₹	*Assets*	₹
A's Capital	1,00,000	Fixed Assets	1,40,000
B's Capital	80,000	Current Assets	60,000
P and L Appropriation A/c			
2021-22	40,000	Drawings — *B*	20,000
	2,20,000		2,20,000

Profit during the year ended 31st March, 2022 was ₹70,000. *A* and *B* share profits in the ratio of 2 : 1. Drawings during the year ended 31st March, 2022 were *A* ₹16,000 and *B* ₹20,000.

[**Ans.** Interest on Capitals : *A* ₹4,800; *B* ₹3,500.]

Adjustment Entries in place of a Single Journal Entry

Q. 68. The Capital Accounts of *P, Q* and *R* stood at ₹2,00,000; ₹1,50,000 and ₹1,00,000 respectively after the necessary adjustments in respect of drawings and net profit for the year ended 31st March, 2019. It was subsequently ascertained that interest on capital @ 10% p.a. was not taken into account while arriving at the divisible profits for the year.

Drawings during the year 2018-19 had been : *P* ₹5,000 per month; *Q* ₹15,000 quarterly and *R* ₹30,000.

The net profit for the year amounted to ₹1,80,000 and partners shared profits and losses in the ratio of 2 : 2 : 1. You are required to pass the necessary journal entries to rectify the lapse in accounting.

[**Ans.** Opening Capitals : *P* ₹1,88,000; *Q* ₹1,38,000 and *R* ₹94,000; Corrected Net Profit ₹1,38,000.]

Hints : (*i*) Entry will be passed for withdrawing the profit of ₹1,80,000 already distributed among the partners.

(*ii*) Entries will be passed for interest on capital ₹42,000.

(*iii*) Entry will be passed for distributing the corrected Net Profit of ₹1,38,000 among the partners.

Q. 69. On 31st March, 2019, the balances in the capital accounts of *A, B* and *C* after making adjustments for profits and drawings were ₹3,20,000, ₹2,40,000 and ₹1,60,000 respectively. Subsequently, it was discovered that the interest on capital and drawings had been omitted.

- The profit for the year ended on 31st March, 2019 was ₹90,000.
- During the year, *A* and *B* each withdrew a sum of ₹48,000 in equal instalments in the middle of every month and *C* withdrew ₹60,000.
- The interest on drawings was to be charged @5% per annum and interest on capital was to be allowed @10% per annum.
- The profit-sharing ratio of the partners was 3 : 2 : 1.

You are required to :

(*i*) Pass the necessary journal entries to rectify the lapse in accounting; and

(*ii*) Prepare the adjusted Capital Accounts of Partners.

[**Ans.** Opening Capitals : *A* ₹3,23,000; *B* ₹2,58,000 and *C* ₹2,05,000; Corrected Net Profit ₹15,300; Balances of Adjusted Capital Accounts : *A* ₹3,13,750; *B* ₹2,39,700 and *C* ₹1,66,550.]

Hints :

(*i*) Entry will be passed for withdrawing the profit of ₹90,000 already distributed among the partners.

(*ii*) Entries will be passed for Interest on Capital ₹78,600 and interest on drawings ₹3,900.

(*iii*) Entry will be passed for distributing the Corrected Net Profit of ₹15,300 among the partners.

Q. 70. *A, B, C* and *D* are partners in a firm. Their respective capitals were ₹4,00,000; ₹3,00,000; ₹2,00,000 and ₹1,00,000. Firm earned a profit of ₹2,50,000 for the year ended 31st March 2022. Profits were distributed in the ratio of their capitals, without providing for the following provisions of the partnership deed :

(*i*) *A*'s guarantee to the firm that the firm would earn a profit of atleast ₹3,00,000. Any shortfall in firm's profits would be personally met by him.

(*ii*) Profits to be shared equally.

You are required to pass the necessary journal entries to rectify the error.

[**Ans.** Shortfall in profit debited to *A*'s Capital A/c ₹50,000.]

Hint : Separate adjusting entries are to be passed.

Guarantee of Minimum Share of Profit

Q. 71 (A). *A, B* and *C* are partners in a firm. Their profit sharing ratio is 3 : 2 : 1. However, *C* is guaranteed a minimum amount of ₹10,000 as share of profits every year. Any deficiency arising on that account shall be met by *A*. The profits for the two years ending 31st March, 2021 and 2022 were ₹30,000 and ₹90,000 respectively. Prepare Profit and Loss Appropriation Account for the two years.

[**Ans.** 1st year ₹10,000 each. 2nd year *A* ₹45,000; *B* ₹30,000 and *C* ₹15,000.]

Q. 71 (B). *X, Y* and *Z* are partners with capitals of ₹4,00,000; ₹3,00,000 and ₹2,00,000 respectively. They charge 8% p.a. interest on their capitals and divide the profits in the ratio of 3 : 2 : 1. *X* has guaranteed that *Z*'s share shall not amount to less than ₹50,000 in any one year.

Their Drawings during the year were ₹50,000; ₹40,000 and ₹35,000 respectively. Net profits for the year before providing interest on capitals was ₹2,52,000. Prepare P & L Appropriation A/c and capital accounts.

[**Ans.** Profits *X* ₹70,000; *Y* ₹60,000; *Z* ₹50,000.]

Q. 72. *S, T, W* and *X* are partners sharing profits in the ratio of 4 : 3 : 2 : 1. *X* is given a guarantee that his share of profits in any given year would be ₹80,000. Deficiency if any, would be borne by other partners equally. The profits for the year ended 31st March, 2022 amounted to ₹6,50,000. Pass necessary entries in the books of the firm.

[**Ans.** Final share in profits : *S* ₹2,55,000; *T* ₹1,90,000; *W* ₹1,25,000 and *X* ₹80,000.]

Q. 73. *A, B* and *C* were partners sharing profits and losses in the ratio of 3 : 2 : 1. Their capitals on 1st April, 2021 were :

A ₹5,00,000; *B* ₹3,00,000 and *C* ₹2,00,000.

A had personally guaranteed that in any year *C*'s share of profit after allowing interest on capital to all partners @8% p.a. and charging interest on drawings @10% p.a. will not be less than ₹1,00,000.

The net profit for the year ended 31st March, 2022, before allowing or charging any interest amounted to ₹4,32,000.

A has withdrawn ₹5,000 at the end of every month.

B has withdrawn ₹15,000 at the end of every quarter.

C has withdrawn ₹60,000 during the year.

Prepare Profit and Loss Appropriation Account for the year 2021-22.

[**Ans.** Share of Profit *A* ₹1,40,000; *B* ₹1,20,000 and *C* ₹1,00,000.]

Q. 74. *A, B* and *C* were in partnership sharing profits in the ratio of 1 : 2 : 3. Their fixed capitals on 1st April, 2021 were : *A* ₹3,00,000; *B* ₹4,50,000 and *C* ₹10,00,000. Their partnership deed provided for the following :

(*i*) *A* provides his personal office to the firm for business use charging yearly rent of ₹1,50,000.

(*ii*) Interest on capital @ 8% p.a. and interest on drawings @ 10% p.a.

(*iii*) *A* was allowed salary @ ₹10,000 per month.

(*iv*) *B* was allowed a commission of 10% of net profit as shown by Profit & Loss Account, after charging such commission.

(*v*) *C* was guaranteed a profit of ₹3,00,000 after making all the adjustments.

The net profit of the firm for the year ended 31st March, 2022 was ₹10,30,000 before making above adjustments.

You are informed that *A* has withdrawn ₹5,000 at the beginning of each month, *B* has withdrawn ₹5,000 at the end of each month and *C* has withdrawn ₹24,000 at the beginning of each quarter.

Prepare Profit and Loss Appropriation Account and Partner's Current Accounts.

[**Ans.** Divisible Profit ₹5,52,000; Share of Profit *A* ₹84,000; *B* ₹1,68,000 and *C* ₹3,00,000. Balances of Current Accounts : *A* ₹3,14,750; *B* ₹2,21,250 and *C* ₹2,78,000.]

Hints : (*i*) Commission to *B* ₹80,000; (*ii*) Total Interest on Drawings ₹12,000.

Q. 75. Ram, Mohan and Sohan were partners. They admit Rakesh as a partner and guaranteed that his share of profit shall not be less than ₹70,000. Profits are to be shared in the ratio of 4 : 3 : 2 : 1 but excess claimed by Rakesh over his normal share has been guaranteed by Ram and Mohan in the ratio of 2 : 1. If total profits were ₹4,00,000, prepare a statement showing distribution.

[**Ans.** Final share in profit is as follows : Ram ₹1,40,000; Mohan ₹1,10,000; Sohan ₹80,000; Rakesh ₹70,000.]

Q. 76. *X* and *Y* were sharing profits in the ratio of 2 : 1. On 1st April, 2021 they admitted *Z* for $\frac{1}{4}$th share in the profits. *Z* is guaranteed a minimum profit of ₹1,00,000 for the year. Any deficiency in *Z*'s share is to be borne by *X* and *Y* in the ratio of 3 : 2. Losses for the year ending 31st March, 2022 amounted to ₹1,20,000. Record necessary entries.

[**Ans.** (*i*) First of all, loss of ₹1,20,000 will be debited to *X, Y* and *Z* in their new profit sharing ratio of 2 : 1 : 1.

(*ii*) Thereafter, *Z*'s deficiency of ₹1,30,000 will be borne by *X* and *Y* in 3 : 2.]

Q. 77. *A, B* and *C* are partners sharing profits in the ratio of 4 : 3 : 2. It was provided that *B*'s share of profit will not be less than ₹1,50,000 per annum. The losses for the year ended 31st March, 2022 were ₹85,000, before allowing interest on Loan of ₹1,00,000 taken from *A* on 1st June, 2021.

You are required to show necessary account for division of loss and pass necessary journal entries.

[**Ans.** (*i*) First of all, loss of ₹90,000 (₹85,000 + Interest ₹5,000) will be debited to *A*, *B* and *C* in 4 : 3 : 2.

(*ii*) Thereafter, *B*'s deficiency of ₹1,80,000 will be be borne by *A* and *C* in 4 : 2.

Q. 78. Ali, Bimal and Deepak are partners in a firm. On 1st April, 2021 their capital accounts stood at ₹4,00,000, ₹3,00,000 and ₹2,00,000 respectively. They shared profits and losses in the proportion of 5 : 3 : 2. Partners are entitled to interest on capital @10% per annum and salary to Bimal and Deepak @₹2,000 per month and ₹3,000 per quarter respectively as per the provisions of the partnership deed.

Bimal's share of profit (excluding interest on capital but including salary) is guaranteed at a minimum of ₹50,000 p.a. Any deficiency arising on that account shall be met by Deepak. The profits of the firm for the year ended 31st March, 2022 amounted to ₹2,00,000. Prepare Profit & Loss Appropriation Account for the year ended on 31st March, 2022.

[**Ans.** Final Share of Profit Ali ₹37,000; Bimal ₹26,000 and Deepak ₹11,000. Deficiency of Bimal borne by Deepak ₹3,800.]

Q. 79. *A*, *B* and *C* entered into a partnership on 1st April, 2021 with capitals of ₹80,000, ₹50,000 and ₹40,000 respectively. Each partner is entitled to interest on his capital @ 8% p.a. *B* is entitled to a salary of ₹8,000 p.a. and *C* a salary of ₹6,000 p.a. They decided to share profits and losses in the ratio of 5 : 3 : 2.

A guaranteed that the firm would earn a profit of ₹60,000 before allowing interest on capital and partners salaries. The actual profit for the year ending 31st March, 2022 before interest and salaries amounted to ₹56,000. Prepare Profit & Loss Appropriation A/c and the Partner's Capital Accounts.

[**Ans.** Balance of Capital Accounts : *A* ₹98,600; *B* ₹71,720 and *C* ₹55,680.]

ADDITIONAL QUESTIONS

Q. 80. Ravi and Tiku are partners in a firm. According to their partnership deed:

(*i*) Interest on capital will be allowed @ 5% per annum.

(*ii*) Interest on drawings will be charged @ 4% per annum.

(*iii*) Each partner will be given a salary of ₹1,000 per month.

(*iv*) Partners will share profits and losses in the ratio of 2 : 1.

Following are the particulars of the capitals and drawings of the partners :

	Ravi	*Tiku*
	₹	₹
Capital (1st April, 2017)	60,000	50,000
Drawings (made on 1st June, 2017)	3,000	6,000

Ravi had taken a loan of ₹10,000 from the firm on which interest of ₹200 was due by him to the firm.

The accounts for the year 2017-18 showed that the firm had made a profit of ₹77,000 before taking into account any interest, partner's salaries and manager's salary of ₹18,000.

You are required to prepare :

(*i*) Profit and Loss Appropriation Account for the year 2017-18,

(*ii*) Partner's Capital Accounts. (*I.S.C. 2019*)

[**Ans.** Share of Profit Ravi ₹20,000 and Tiku ₹10,000; Capital Accounts : Ravi ₹91,700 and Tiku ₹68,300.]

Hints :

(*i*) Net Profit as per P & L A/c ₹59,200 (*i.e.*, ₹77,000 + ₹200 – ₹18,000).

(*ii*) Interest on Loan ₹200 will also be debited to Ravi's Capital A/c.

Q. 81. Asif and Ravi are partners in a firm sharing profits and losses in the ratio of 3 : 2. Their fixed capitals as on 1st April, 2016, were ₹6,00,000 and ₹4,00,000 respectively.

Their partnership deed provided for the following :

(*a*) Partners are to be allowed interest on their capitals @ 10% per annum.

(*b*) They are to be charged interest on drawings @ 4% per annum.

(*c*) Asif is entitled to a salary of ₹2,000 per month.

(*d*) Ravi is entitled to a commission of 5% of the correct net profit of the firm before charging such commission.

(*e*) Asif is entitled to a rent of ₹3,000 per month for the use of his premises by the firm.

The net profit of the firm for the year ended 31st March, 2017, before providing for any of the above clauses was ₹4,00,000.

Both partners withdrew ₹5,000 at the beginning of every month for the entire year.

You are required to prepare a Profit and Loss Appropriation Account for the year ended 31st March, 2017. (*I.S.C. 2018*)

[**Ans.** Divisible Profit ₹2,24,400.]

Hint. Commission 5% on ₹3,64,000 = ₹18,200.

Q. 82. Shankar and Manu are partners in a firm. On 1st April, 2014, their fixed capital accounts showed a balance of ₹2,00,000 and ₹4,00,000 respectively.

On this date, their current account balances were ₹50,000 and ₹1,00,000 respectively.

On 1st January, 2015, Shankar introduced additional capital of ₹2,00,000 while Manu gave a loan of ₹1,50,000 to the firm.

The clauses of their partnership deed provided for :

(*a*) Interest on capital to be allowed at the rate of 10% per annum.

(*b*) Interest on drawings to be charged at the rate of 12% per annum.

(*c*) Profits to be shared by them in the ratio of 3 : 2.

(*d*) 10% of the correct net profit to be transferred to General Reserve.

During the financial year 2014-15, both partners withdrew ₹6,000 each at the beginning of every quarter.

The net profit of the firm, before any interest, for the financial year 2014-15 was ₹5,00,000.

You are required to prepare for the year 2014-15 :

(*i*) Profit and Loss Appropriation Account.
(*ii*) Partners' Fixed Capital Accounts.
(*iii*) Partners' Current Accounts.
(*iv*) Partner's Loan Account. *(I.S.C. 2016)*

[**Ans.** Divisible Profit ₹3,86,575; Current A/cs balances : Shankar ₹2,81,145 and Manu ₹2,68,830.]

Q. 83. *X, Y* and *Z* are in the partnership and on 1st April, 2021, their respective capitals were ₹2,00,000; ₹1,20,000 and ₹1,00,000. *Y* is entitled to a salary of ₹25,000 and *Z* ₹20,000 per annum, payable before division of profits. Interest is allowed on capital at 5% per annum but is not charged on drawings. Of the net divisible profits of the first ₹1,00,000; *X* is entitled to 40 per cent; *Y* to 35 per cent and *Z* to 25 per cent, over that amount profits are shared equally. The profit for the year ended 31st March, 2022, after debiting partnership salaries, but before charging interest on capitals, was ₹1,81,000 and the partners had drawn ₹8,000 each. Prepare partners' capital accounts for the year.

[**Ans.** Divisible Profits ₹1,60,000; Balance of Capital Accounts *X* ₹2,62,000; *Y* ₹1,98,000; *Z* ₹1,62,000.]

Q. 84. *A* and *B* are partners in a firm. *A* is to get a commission of 10% of net profit before charging any commission. *B* is to get a commission of 10% on net profit after charging all commissions. Net profit before charging any commission was ₹55,000. Find out the commission of *A* and *B*.

[**Ans.** *A*'s commission ₹5,500; *B*'s commission ₹4,500.]

Q. 85. On 1st April, 2021 the balances of *A* and *B* were as follows :—

	Capital Account	*Current Account*
	₹	₹
A	1,00,000	(Cr.) 8,420
B	40,000	(Dr.) 3,200

On 1st July, 2021, *A* withdrew ₹20,000 from his capital and *B* introduced ₹10,000 as further capital on the same date. According to the deed, interest on capitals is to be allowed at 8% p.a. but no interest is to be allowed or charged on current account balances and drawings. *A* is entitled to $\frac{3}{5}$ and *B* $\frac{2}{5}$ of the profit. The manager of the firm is entitled to a commission of 10% of the profit before any adjustment is made according to the deed. For the year ended 31st March, 2022, the profit was ₹40,000 and the drawings of *A* and *B* were ₹12,000 and ₹10,000 respectively. Prepare the P & L Appropriation A/c, Capital Accounts and Current Accounts.

[**Ans.** Manager's commission ₹4,000; Divisible Profit ₹25,400; Current Account balances : *A* ₹18,460 (Cr.) and *B* ₹760 (Cr.); Capital Account balances : *A* ₹80,000 and *B* ₹50,000.]

Q. 86. *A* and *B* are partners in a firm sharing profits and losses in the ratio of 3 : 2. The balance in their capital and current accounts as on 1-4-2021 were as under :

	A	B
	₹	₹
Capital Account	40,000	20,000
Current Account (Cr.)	16,000	12,000

The partnership deed provided that *A* is to be paid salary @ ₹500 p.m. whereas *B* is to get commission of ₹4,000 for the year.

Interest on capital is to be allowed @ 6% p.a. The drawings of *A* and *B* for the year were ₹5,000 and ₹2,000, respectively. Interest on drawings for *A* and *B* works out at ₹225 and ₹75 respectively. The net profit of the firm for the year ended 31st March, 2022 before making these adjustments was ₹35,700.

Prepare the Profit and Loss Appropriation Account and the Partners Capital and Current Accounts.

[**Ans.** Divisible Profits ₹22,400; Balances of Capital Accounts : *A* ₹40,000; *B* ₹20,000. Balances of Current Accounts :— *A* ₹32,615; *B* ₹24,085.]

Q. 87. Calculate the interest on Drawings of Tarun @ 8% p.a. for the year ended 31st March 2022 in each of the following alternative cases :

Case (*a*) if his drawings during the year were ₹60,000;

Case (*b*) if he withdrew ₹5,000 p.m. in the beginning of every month;

Case (*c*) if he withdrew ₹5,000 p.m. at the end of every month;

Case (*d*) if he withdrew ₹5,000 p.m.;

Case (*e*) if he withdrew the following amounts as under :

2021 : June 1 ₹10,000; Aug. 31 ₹12,000; Nov. 1 ₹16,000; Dec. 31 ₹13,000;

2022 : Feb. 1 ₹9,000.

[**Ans.** Case (*a*) ₹2,400; Case (*b*) ₹2,600; Case (*c*) ₹2,200; Case (*d*) ₹2,400; Case (*e*) ₹2,140.]

Q. 88. *A*, *B* and *C* have Capitals of ₹60,000, ₹30,000 and ₹20,000 respectively on 1st April, 2021, on which they are entitled to interest @ 6% p.a. They share profits in the ratio of 5 : 3 : 2. *A* is entitled to receive a salary of ₹500 per month. Drawings during the year were as follows :—

	A	B	C
	₹	₹	₹
1st June, 2021	2,000	2,000	1,000
1st Oct., 2021	1,000	1,500	1,000
1st Dec., 2021	500	1,000	500

The rate of interest on Drawings is 6% p.a. Profit for the year ended 31st March, 2022 was ₹24,605 before charging salary, interest on Capital and Drawings. Assuming that the Capitals are (*a*) Fixed, (*b*) Floating, show the Partners' Capital Accounts, Current Accounts and Profit and Loss Appropriation Account.

[**Ans.** Interest on Drawings *A* ₹140; *B* ₹165 and *C* ₹90. Divisible Profits ₹12,400. Current A/c balances *A* ₹12,160; *B* ₹855; *C* ₹1,090.]

Q. 89. *A*, *B* and *C* are in partnership sharing profits and losses in the ratio of 2 : 1 : 1. It is agreed that interest on Capital will be allowed @ 5 per cent per annum

and interest on drawings will be charged @ 4 per cent per annum. No interest will be allowed or charged on Current Accounts.

The following are the particulars of the Capital, Current and Drawings Accounts of the partners :

	A ₹	*B* ₹	*C* ₹
Capital A/cs (1.4.2021)	1,50,000	80,000	60,000
Current A/cs (1.4.2021)	20,000	10,000	Dr. (10,000)
Drawings	30,000	20,000	20,000
Interest on Drawings (2021-22)	1,000	280	700

The draft accounts for the year ending 31.3.2022 showed a net profit of ₹ 1,20,000 before taking into account interest on Capital and drawings and subject to following rectification of errors :

(1) Life insurance premium of *A* amounting to ₹1,500 paid by the firm on 31st March, 2022 has been charged to Miscellaneous Expenditure Account.

(2) Repairs of machinery amounting to ₹20,000 has been debited to Plant Account and depreciation thereon charged @ 20 per cent.

(3) An item in the inventory was valued at ₹45,000 but was subsequently found to be worth ₹30,000 only.

You are required to prepare the Profit & Loss Appropriation Account for the year ended 31st March, 2022 and the Partner's Current Accounts for the year.

[**Ans.** Divisible Profits ₹77,980; Current A/cs : *A* ₹33,990 (Cr.); *B* ₹13,215 (Cr.) and *C* ₹8,205 (Dr.).]

Q. 90. *X*, *Y* and *Z* contribute ₹3,00,000, ₹2,00,000 and ₹1,00,000 respectively by way of capital on which they agree to allow interest at 12% p.a. They share profits and losses in the ratio of 5 : 3 : 2. Profit for the year ended 31st March 2022 is ₹60,000 before allowing interest on capitals. Prepare a Profit & Loss Appropriation Account if (*i*) partnership deed is silent as to the treatment of interest as a charge or appropriation, and (*ii*) partnership deed provides for interest even if it involves the firm in loss.

[**Ans.** Case (*i*) Interest on capital *X* ₹30,000; *Y* ₹20,000 and *Z* ₹10,000. Case (*ii*) Loss *X* ₹6,000; *Y* ₹3,600 and *Z* ₹2,400.]

Adjustments in the Closed Accounts

Q. 91. Vinay, Usha and Punit are partners in a firm. They have been sharing profits and losses in the ratio of 3 : 4 : 1.

Punit wants the profits to be shared equally amongst the partners. He further wants change in profit sharing ratio to be applicable retrospectively for the last two years. Vinay and Usha have no objection to this.

The profits for the last two years were ₹70,000 and ₹50,000.

You are required to record the adjustment by means of a single journal entry.

(I.S.C. 2019)

[**Ans.** Vinay's Capital A/c	Dr.	5,000	
Usha's Capital A/c	Dr.	20,000	
To Punit's Capital A/c			25,000]

Q. 92. Vineet and Pawan are partners sharing profits and losses in the ratio of 3 : 2. During the year 2016-17, Vineet had made drawings of ₹10,000 on which, as per the partnership deed, interest @5% p.a. had to be charged but was omitted while distributing the profit.

You are required to pass an adjusting journal entry to rectify the lapse in accounting.

(ISC Sample Paper, 2018)

[**Ans.** Vineet's Capital A/c	Dr.	100	
To Pawan's Capital A/c			100]

Q. 93. Raja, Roopa and Mala sharing profits and losses equally have fixed capitals of ₹12,00,000 ₹9,00,000 and ₹6,00,000 respectively. For the year ended 31st March, 2022, interest was credited to them @ 6% instead of 5% p.a. Give adjusting entry.

[**Ans.**		₹	₹
Raja's Current A/c	Dr.	3,000	
To Mala's Current A/c			3,000]

Q. 94. *P* and *Q* were partners in a firm sharing profits in 7 : 3 ratio. Their fixed capitals were *P* ₹5,00,000 and *Q* ₹8,00,000. For the year ended 31st March, 2022, interest on capital was credited @ 12% instead of 10%. Show the necessary adjusting entry for the rectification of the error. Also show the working notes clearly.

[**Ans.**		₹	₹
Q's Current A/c	Dr.	8,200	
To *P*'s Current A/c			8,200]

Q. 95. *A*, *B* and *C* are partners. Their fixed capitals as on 31st March, 2022 were *A* ₹2,00,000, *B* ₹3,00,000 and *C* ₹4,00,000. Profits for the year ended 31st March, 2022, amounting to ₹1,80,000 were distributed. Give the necessary adjusting entry in each of the following alternative cases :

Case (*a*) Interest on capital was credited @ 8% p.a. though there was no such provision in the partnership deed.

Case (*b*) Interest on capital was not credited @ 8% p.a. though there was such provision in the partnership deed.

Case (*c*) Interest on capital was credited @ 8% p.a. instead of 10% p.a.

Case (*d*) Interest on capital was credited @ 10% p.a. instead of 8% p.a.

[**Ans.** Debit *C*'s Current A/c and Credit *A*'s Current A/c with ₹8,000;
Debit *A*'s Current A/c and Credit *C*'s Current A/c with ₹8,000;
Debit *A*'s Current A/c and Credit *C*'s Current A/c with ₹2,000;
Debit *C*'s Current A/c and Credit *A*'s Current A/c with ₹2,000;]

Q. 96. *E*, *F* and *G* were partners in a firm sharing profits in the ratio of 3 : 2 : 1. After division of the profits for the year ended 31-3-2022 their capitals were : *E* ₹2,95,000; *F* ₹3,30,000; and *G* ₹3,35,000. During the year they withdrew ₹40,000 each. The profit of the year was ₹1,80,000. The partnership deed provided that interest on capital will be allowed @ 12% p.a. While preparing the final accounts, interest on partners' capital was not allowed.

You are required to calculate the capital of *E*, *F* and *G* as on 1-4-2021 and pass the necessary adjustment entry for providing interest on capital. Show your workings clearly.

[**Ans.** Opening Capitals *E* ₹2,45,000; *F* ₹3,10,000 and *G* ₹3,45,000. Adjusting Entry :

E's Capital A/c	Dr.	24,600	
To *F*'s Capital A/c			1,200
To *G*'s Capital A/c			23,400]

Q. 97. *A* and *B* are partners in a business. Their capitals at the end of the year were ₹6,40,000 and ₹4,60,000 respectively. During the year ending 31st March, 2022, *A*'s drawings and *B*'s drawings were ₹1,20,000 and ₹1,40,000 respectively. Profits (before charging interest on capital) during the year were ₹4,00,000. Calculate interest on capital @ 12% p.a. for the year ending 31st March, 2022.

[**Ans.** Interest on Capitals : *A* ₹67,200; *B* ₹48,000.]

Q. 98. Alex, John and Sam are partners in a firm. Their capital accounts on 1st April, 2011, stood at ₹1,00,000, ₹80,000 and ₹60,000 respectively.

Each partner withdrew ₹5,000 during the financial year 2011-12.

As per the provisions of their partnership deed :

(*a*) John was entitled to a salary of ₹1,000 per month.

(*b*) Interest on capital was to be allowed @10% per annum.

(*c*) Interest on drawings was to be charged @4% per annum.

(*d*) Profits and losses were to be shared in the ratio of their capitals.

The net profit of ₹75,000 for the year ended 31st March 2012, was divided equally amongst the partners without providing for the terms of the deed.

You are required to pass a Single Adjusting Journal Entry to rectify the error. (Show the working clearly) *(I.S.C. 2013)*

SOLUTION :

STATEMENT OF ADJUSTMENTS

Particulars	*Alex*	*John*	*Sam*
	₹	₹	₹
1. Amount which should have been credited :			
Salary		12,000	
Interest on Capital	10,000	8,000	6,000
Profit (₹75,000 – ₹12,000 – ₹24,000 + ₹300 for interest on drawings = ₹39,300) in 5 : 4 : 3	16,375	13,100	9,825
Cr.	26,375	33,100	15,825
2. Amount which should have been debited :			
Interest on Drawings	100	100	100
Profit already distributed equally	25,000	25,000	25,000
Dr.	25,100	25,100	25,100
Net Effect	(Cr.) 1,275	(Cr.) 8,000	(Dr.) 9,275

ADJUSTMENT ENTRY

			₹	₹
2012				
April 1	Sam's Capital A/c	Dr.	9,275	
	To Alex's Capital A/c			1,275
	To John's Capital A/c			8,000
	(Adjustment for salary, interest on capital, interest on drawing and wrong distribution of profit)			

Q. 99. *A*, *B* and *C* were partners in a firm. On 1st April, 2021 their capitals stood as ₹5,00,000; ₹2,50,000 and ₹2,50,000 respectively. As per provisions of the partnership deed :

(*i*) *C* was entitled for a salary of ₹5,000 per month.
(*ii*) *A* was entitled for a commission of ₹80,000 p.a.
(*iii*) Partners were entitled to interest on capital @6% p.a.
(*iv*) Partners will share profits in the ratio of capitals.

Net profit for the year ended 31.03.2022 was ₹3,00,000 which was distributed equally, without taking into consideration the above provisions. Showing your workings clearly, pass necessary adjustment entry for the above.

[**Ans.**	*B*'s Capital A/c	Dr.	60,000	
	To *A*'s Capital A/c			60,000]

Guarantee of Profit to a Partner

Q. 100. Peter, Max and Som were partners in a firm sharing profits and losses in the ratio of 4 : 2 : 1. Their fixed capitals were ₹40,000, ₹30,000 and ₹30,000, respectively.

Som was guaranteed a profit of ₹39,000 by the firm.

It was decided that any loss arising because of the guarantee would be shared by Peter and Max equally.

The net profit of the firm for the year ended 31st March, 2018, was ₹1,47,000.

You are required to prepare the Profit and Loss Appropriation Account for the year 2017-18, showing the distribution of profits. *(I.S.C. 2019)*

[**Ans.** Share of Profit : Peter ₹75,000; Max ₹33,000 and Som ₹39,000.]

Q. 101. *A*, *B* and *C* are partners in a firm sharing profits in the ratio of 2 : 2 : 1. According to the terms of the partnership agreement *C* has to get a minimum of ₹6,000 irrespective of the profits of the firm. Any excess payable to *C* on account of such guarantee shall be borne by *A*. Profits earned during the year ended 31st March, 2022 were ₹25,000. Pass journal entries in the books of the firm.

[**Ans.** Share of Profits *A* ₹9,000; *B* ₹10,000 and *C* ₹6,000]

Q. 102. *A*, *B* and *C* are partners sharing profits in the ratio of 5 : 4 : 1. *C* is given a guarantee that his share of profits in any year will not be less than ₹20,000. The profit for the year ending 31st March 2022 amounts to ₹1,40,000. Amount of shortfall in the profits given to *C* will be borne by *A* and *B* in the ratio of 3 : 2. Pass necessary journal entry regarding deficiency borne by *A* and *B*.

[Ans. *A*'s Capital A/c	Dr.	3,600	
B's Capital A/c	Dr.	2,400	
To *C*'s Capital A/c			6,000]

Q. 103. *X, Y* and *Z* were in partnership. *X* and *Y* sharing profits in the proportion of 2 : 1 and *Z* receiving a salary of ₹1,790 per month plus 5% of the profit after charging his salary and commission or $\frac{1}{5}$th of the profit of the firm whichever is more. Any excess of the latter over the former received by *Z* is, under the partnership deed, to be borne by *X*. The profit for the year ended 31st March, 2022 amounted to ₹1,28,520 after charging *Z*'s salary.

Prepare the Profit and Loss Appropriation Account showing the division of the profit of the year.

[**Ans.** Profit *X* ₹79,200; *Y* ₹40,800 and *Z* ₹30,000.]

Q. 104. On 1st April, 2021 *A, B* and *C* started a business in partnership and contributed ₹1,00,000, ₹80,000 and ₹60,000 respectively, as their capitals. They agreed to share profits and losses in the ratio of 3 : 2 : 1 after allowing interest on capital @ 10% p.a. and charging interest on drawings @ 12% p.a. The drawings of the partners during the year ended 31st March, 2022 were : *A* ₹12,000; *B* ₹15,000 and *C* ₹6,000.

C, to whom a salary of ₹1,000 p.m. was payable, had guaranteed that the firm would earn a profit of ₹75,000 before charging or allowing interest and salary payable to the partners. The actual profit before interest and salary amounted to ₹70,000.

Prepare Profit and Loss Appropriation A/c and the Partner's Capital Accounts.

[**Ans.** Share of Profit *A* ₹20,490; *B* ₹13,660 and *C* ₹6,830; Balance of Capital Accounts : *A* ₹1,17,770; *B* ₹85,760 and *C* ₹73,470.]

Hint : Firm's profit is ₹70,000 (*i.e.*, ₹5,000 less than the amount guaranteed by *C*). As such ₹5,000 will be debited to *C*'s Capital A/c and credited to P & L App. A/c.

Q. 105. Hill, Vale and Dale are in partnership, sharing profits and losses in the ratio of 2 : 2 : 1 respectively. Interest is charged on Partners' Drawings @ 6% p.a. and credited to Partners' Capital Account Balances @ 6% p.a.

Vale is the firm's Marketing Manager and for his specialised services, he is credited with a salary of ₹2,000 per quarter.

During the year ended 31st March, 2022 the net profit of the firm was ₹62,000 and the partners' drawings were :

		₹
Hill	:	12,000
Vale	:	8,000
Dale	:	8,000

In each case, the above drawings were made in two equal instalments on 30th September, 2021 and 31st March, 2022.

On 30th September, 2021, the firm agreed that Hill should withdraw ₹10,000 from his capital account and the Dale should subscribe a similar amount to his capital account.

The balances of the partners' accounts on 1st April, 2021 were :

All Credit Balances

		Capital Accounts	*Current Accounts*
		₹	₹
Hill	:	80,000	6,400
Vale	:	70,000	5,600
Dale	:	60,000	4,800

Transfer 5% of the net profit to the Reserve Fund of the firm.

Required :

(*i*) Prepare the firm's Profit and Loss Appropriation Account for the year ended 31st March, 2022.

(*ii*) Prepare the Partners' Capital and Current Accounts for the year ended 31st March, 2022.

SOLUTION :

In the Books of Hill, Vale and Dale

PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2022* Cr.

Particulars		₹	*Particulars*		₹
To Reserve Fund (5% of ₹62,000)		3,100	By Profit and Loss A/c — Net Profit		62,000
To Interest on Capital A/c(1)			By Interest on Drawings A/c(2)		
Hill	4,500		Hill	180	
Vale	4,200		Vale	120	
Dale	3,900	12,600	Dale	120	420
To Salary A/c — Vale (₹2,000 × 4)		8,000			
To Net Profit transferred to :					
Hill's Current A/c (2/5)	15,488				
Vale's Current A/c (2/5)	15,488				
Dale's Current A/c (1/5)	7,744	38,720			
		62,420			62,420

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Date	*Particulars*	*Hill*	*Vale*	*Dale*	*Date*	*Particulars*	*Hill*	*Vale*	*Dale*
2021		₹	₹	₹	2021		₹	₹	₹
Sep. 30	To Bank A/c	10,000	—	—	April 1	By Balance b/d	80,000	70,000	60,000
2022					Sep. 30	By Bank A/c	—	—	10,000
Mar. 31	To Balance c/d	70,000	70,000	70,000					
		80,000	70,000	70,000			80,000	70,000	70,000

Dr. PARTNERS' CURRENT ACCOUNTS Cr.

Date	*Particulars*	*Hill*	*Vale*	*Dale*	*Date*	*Particulars*	*Hill*	*Vale*	*Dale*
2022		₹	₹	₹	2021		₹	₹	₹
Mar. 31	To Drawings A/c	12,000	8,000	8,000	April 1	By Bal. b/d	6,400	5,600	4,800
					2022				
Mar. 31	To Interest on Drawings A/c	180	120	120	Mar. 31	By Interest on Capital A/c	4,500	4,200	3,900
Mar. 31	To Bal. c/d	14,208	25,168	8,324	Mar. 31	By Salary		8,000	—
					Mar. 31	By P & L Appr. A/c (Profit)	15,488	15,488	7,744
		26,388	33,288	16,444			26,388	33,288	16,444

Working Notes :

(1) Interest on Capital :

		₹
Hill :	on ₹80,000 for 6 months	2,400
	on ₹70,000 for 6 months	2,100
		4,500
Vale :	on ₹70,000 for 1 year	4,200
Dale :	on ₹60,000 for 6 months	1,800
	on ₹70,000 for 6 months	2,100
		3,900

(2) Interest on Drawings :

Hill :	on ₹6,000 for 6 months	180
	on ₹6,000 for 0 months	0
		180
Vale and Dale :	on ₹4,000 for 6 months	120
	on ₹4,000 for 0 months	0
		120

Q. 106. Anwar, Biswas and Divya are partners in a firm. Their Capital Accounts stood at ₹8,00,000; ₹6,00,000 and ₹4,00,000 respectively on 1st April, 2021. They shared profits and losses in the ratio of 3 : 2 : 1 respectively. Partners are entitled to interest on capital @6% per annum and salary to Biswas and Divya @₹4,000 per month and ₹6,000 per quarter respectively as per the provisions of Partnership Deed.

Biswas's share of profit including interest on capital but excluding salary is guaranteed at a minimum of ₹82,000 p.a. Any deficiency arising on that account shall be met by Divya. Profit for the year ended 31st March, 2022 amounted to ₹3,12,000. Prepare Profit and Loss Appropriation Account for the year ended 31st March, 2022.

[**Ans.** Final Share of Profit : Anwar ₹66,000; Biswas ₹46,000 and Divya ₹20,000. Deficiency of Biswas borne by Divya ₹2,000.]

Q. 107. Ankur, Bhavna and Disha are partners in a firm. On 1st April 2021, the balance in their capital accounts stood at ₹14,00,000, ₹6,00,000 and ₹4,00,000 respectively. They shared profits in the proportion of 7 : 3 : 2 respectively. Partners are

entitled to interest on capital @6% per annum and salary to Bhavna @₹50,000 p.a. and a commission of ₹3,000 per month to Disha as per the provisions of the Partnership Deed.

Bhavna's share of profit (excluding interest on capital) is guaranteed at not less than ₹1,70,000 p.a. Disha's share of profit (including interest on capital but excluding salary) is guaranteed at not less than ₹1,50,000 p.a. Any deficiency arising on that account shall be met by Ankur. The profits of the firm for the year ended 31st March, 2022 amounted to ₹9,50,000.

Prepare 'Profit and Loss Appropriation Account' for the year ended 31st March, 2022.

[**Ans.** Share of Profit : Ankur — ₹4,14,000; Bhavna — ₹1,80,000 and Disha — ₹1,26,000; Deficiency of Disha borne by Ankur ₹6,000]

MULTIPLE CHOICE QUESTIONS

Select the Best Alternate and tally your answer with the Answers given at the end of the book :

(i) Features or Characteristics of Partnership

1. Features of a partnership firm are :
   (A) Two or more persons are carrying common business under an agreement.
   (B) They are sharing profits and losses in the fixed ratio.
   (C) Business is carried by all or any of them acting for all as an agent.
   (D) All of the above.

HOTS

2. Following are essential elements of a partnership firm except :
   (A) Atleast two persons
   (B) There is an agreement between all partners
   (C) Equal share of profits and losses
   (D) Partnership agreement is for some business.

HOTS

3. In case of partnership the act of any partner is :
   (A) Binding on all partners
   (B) Binding on that partner only
   (C) Binding on all partners except that particular partner
   (D) None of the above

HOTS

4. Which of the following statement is true?
   (A) a minor cannot be admitted as a partner
   (B) a minor can be admitted as a partner, only into the benefits of the partnership
   (C) a minor can be admitted as a partner but his rights and liabilities are same of adult partner
   (D) none of the above

5. Oustensible partners are those who
   (A) do not contribute any capital but get some share of profit for lending their name to the business
   (B) contribute very less capital but get equal profit
   (C) do not contribute any capital and without having any interest in the business, lend their name to the business
   (D) contribute maximum capital of the business

HOTS

6. Sleeping partners are those who
   (A) take active part in the conduct of the business but provide no capital. However, salary is paid to them.
   (B) do not take any part in the conduct of the business but provide capital and share profits and losses in the agreed ratio
   (C) take active part in the conduct of the business but provide no capital. However, share profits and losses in the agreed ratio.
   (D) do not take any part in the conduct of the business and contribute no capital. However, share profits and losses in the agreed ratio.
7. The relation of partner with the firm is that of :
   (A) An Owner (B) An Agent
   (C) An Owner and an Agent (D) Manager
8. What should be the minimum number of persons to form a Partnership :
   (A) 2 (B) 7
   (C) 10 (D) 20
9. Number of partners in a partnership firm may be :
   (A) Maximum Two (B) Maximum Ten
   (C) Maximum One Hundred (D) Maximum Fifty
10. Liability of partner is :
   (A) Limited (B) Unlimited
   (C) Determined by Court (D) Determined by Partnership Act
11. Which one of the following is NOT an essential feature of a partnership?
   (A) There must be an agreement
   (B) There must be a business
   (C) The business must be carried on for profits
   (D) The business must be carried on by all the partners

HOTS

12. *X*, *Y* and *Z* are partners sharing profits and losses equally. Their capital balances on March, 31, 2021 are ₹80,000, ₹60,000 and ₹40,000 respectively. Their personal assets are worth as follows : *X* — ₹20,000, *Y* — ₹15,000 and *Z* — ₹10,000. The extent of their liability in the firm would be :
   (A) *X* — ₹80,000 : *Y* — ₹60,000 : and *Z* — ₹40,000
   (B) *X* — ₹20,000 : *Y* — ₹15,000 : and *Z* — ₹10,000

(C) X— ₹1,00,000 : Y— ₹75,000 : and Z— ₹50,000
(D) Equal

13. Every partner is bound to attend diligently to his .... in the conduct of the business.
(A) Rights
(B) Meetings
(C) Capital
(D) Duties

(ii) Partnership Deed

HOTS

14. Forming a Partnership Deed is :
(A) Mandatory
(B) Mandatory in Writing
(C) Not Mandatory
(D) None of the Above

HOTS

15. Partnership Deed is also called ....
(A) Prospectus
(B) Articles of Association
(C) Principles of Partnership
(D) Articles of Partnership

HOTS

16. Which of the following is not incorporated in the Partnership Act?
(A) Profit and loss are to be shared equally
(B) No interest is to be allowed on capital
(C) All loans are to be allowed interest @6% p.a.
(D) All drawings are to be charged interest

17. When is the Partnership Act enforced?
(A) When there is no partnership deed
(B) Where there is a partnership deed but there are differences of opinion between the partners
(C) When capital contribution by the partners varies
(D) When the partner's salary and interest on capital are not incorporated in the partnership deed

18. In the absence of Partnership Deed, the interest is allowed on partner's capital:
(A) @ 6% p.a.
(B) @ 10% p.a.
(C) @ 12% p.a.
(D) No interest is allowed
(C.B.S.E. Sample Paper 2021)

19. In the absence of a partnership deed, the allowable rate of interest on partner's loan account will be :
(A) 6% Simple Interest
(B) 6% p.a. Simple Interest
(C) 12% Simple Interest
(D) 12% Compounded Annually

20. *A* and *B* are partners in partnership firm without any agreement. *A* has given a loan of ₹50,000 to the firm. At the end of year loss was incurred in the business. Following interest may be paid to *A* by the firm :
(A) @5% Per Annum
(B) @ 6% Per Annum

(C) @ 6% Per Month
(D) As there is a loss in the business, interest can't be paid

HOTS

21. *A* and *B* are partners in a pertnership firm without any agreement. *A* has withdrawn ₹50,000 out of his Capital as drawings. Interest on drawings may be charged from *A* by the firm :

(A) @ 5% Per Annum (B) @ 6% Per Annum
(C) @ 6% Per Month (D) No interest can be charged

22. *A* and *B* are partners in a partnership firm without any agreement. *A* devotes more time for the firm as compare to *B*. *A* will get the following commission in addition to profit in the firm's profit :

(A) 6% of profit (B) 4% of profit
(C) 5% of profit (D) None of the above

23. In the absence of partnership deed, the following rule will apply :

(A) No interest on capital
(B) Profit sharing in capital ratio
(C) Profit based salary to working partner
(D) 9% p.a. interest on drawings

24. In the absence of agreement, partners are not entitled to :

(A) Salary (B) Commission
(C) Equal share in profit (D) Both (*a*) and (*b*)

25. Interest on capital will be paid to the partners if provided for in the partnership deed but only out of :

(A) Profits (B) Reserves
(C) Accumulated Profits (D) Goodwill

26. Which one of the following items cannot be recorded in the profit and loss appropriation account?

(A) Interest on capital (B) Interest on drawings
(C) Rent paid to partners (D) Partner's salary

27. If any loan or advance is provided by partner then, balance of such Loan Account should be transferred to :

(A) B/S Assets side (B) B/S Liability Side
(C) Partner's Capital A/c (D) Partner's Current A/c

28. *A*, *B* and *C* were Partners with capitals of ₹50,000; ₹40,000 and ₹30,000 respectively carrying on business in partnership. The firm's reported profit for the year was ₹80,000. As per provision of the Indian Partnership Act, 1932, find out the share of each partner in the above amount after taking into account that no interest has been provided on an advance by *A* of ₹20,000 in addition to his capital contribution.

(A) ₹26,267 for Partner *B* and *C* and ₹27,466 for Partner *A*.
(B) ₹26,667 each partner.
(C) ₹33,333 for *A* ₹26,667 for *B* and ₹20,000 for *C*.
(D) ₹30,000 each partner.

29. *X*, *Y* and *Z* are partners in a firm. At the time of division of profit for the year, there was dispute between the partners. Profit before interest on partner's capital was ₹6,000 and *Y* determined interest @24% p.a. on his loan of ₹80,000. There was no agreement on this point. Calculate the amount payable to *X*, *Y* and *Z* respectively.

(A) ₹2,000 to each partner.

(B) Loss of ₹4,400 for *X* and *Z*; *Y* will take ₹14,800.

(C) ₹400 for *X*, ₹5,200 for *Y* and ₹400 for *Z*.

(D) None of the above.

30. *X*, *Y* and *Z* are partners in a firm. At the time of division of profit for the year there was dispute between the partners. Profit before interest on partner's capital was ₹6,00,000 and *Z* demanded minimum profit of ₹5,00,000 as his financial position was not good. However, there was no written agreement on this point.

(A) Other partners will pay *Z* the minimum profit and will share the loss equally.

(B) Other partners will pay *Z* the minimum profit and will share the loss in capital ratio.

(C) *X* and *Y* will take ₹50,000 each and *Z* will take ₹5,00,000.

(D) ₹2,00,000 to each of the partners.

31. On 1st June, 2018 a partner introduced in the firm additional capital ₹50,000. In the absence of partnership deed, on 31st March, 2019 he will receive interest :

(A) ₹3,000 (B) Zero

(C) ₹2,500 (D) ₹1,800

32. On 1st January 2019, a partner advanced a loan of ₹1,00,000 to the firm. In the absence of agreement, interest on loan on 31st March, 2019 will be :

(A) Nil (B) ₹1,500

(C) ₹3,000 (D) ₹6,000

33. A partner introduced additional capital of ₹30,000 and advanced a loan of ₹40,000 to the firm at the beginning of the year. Partner will receive year's interest :

(A) ₹4,200 (B) ₹2,400

(C) Nil (D) ₹1,800

34. In the absence of partnership deed, partners share profits or losses :

(A) In the ratio of their Capitals

(B) In the ratio decided by the court

(C) Equally

(D) In the ratio of time devoted

35. In the absence of Partnership Deed :

(A) Interest will not be charged on partner's drawings

(B) Interest will be charged @ 5% p.a. on partner's drawings

(C) Interest will be charged @ 6% p.a. on partner's drawings

(D) Interest will be charged @ 12% p.a. on partner's drawings

36. In the absence of express agreement, interest @ 6% p.a. is provided :

(A) On opening balance of partner's capital accounts

(B) On closing balance of partner's capital accounts

(C) On loan given by partners to the firm

(D) On opening balance of partner's current accounts

37. Which of the following items is not dealt through Profit and Loss Appropriation Account?

(A) Interest on Partner's Loan (B) Partner's Salary
(C) Interest on Partner's Capital (D) Partner's Commission

(C.B.S.E. Sample Paper, 2020)

HOTS

38. Is rent paid to a partner appropriation of profits?

(A) It is appropriation of profit
(B) It is not appropriation of profit
(C) If partner's contribution as capital is maximum
(D) If partner is a working partner.

(iii) Calculation of Profit and Division of Profit among partners

39. Sarvesh, Sriniketan and Srinivas are partners in the ratio of 5 : 3 : 2. If Sriniketan's share of profit at the end of the year amounted to ₹1,50,000, what will be Sarvesh's share of profits?

(A) ₹5,00,000. (B) ₹1,50,000.
(C) ₹3,00,000. (D) ₹2,50,000.

(C.B.S.E. Sample Paper, 2021)

40. According to Profit and Loss Account, the net profit for the year is ₹1,50,000. The total interest on partner's capital is ₹18,000 and interest on partner's drawings is ₹2,000. The net profit as per Profit and Loss Appropriation Account will be :

(A) ₹1,66,000 (B) ₹1,70,000
(C) ₹1,30,000 (D) ₹1,34,000

41. According to Profit and Loss Account, the net profit for the year is ₹4,20,000. Salary of a partner is ₹5,000 per month and the commission of another partner is ₹10,000. The interest on drawings of partners is ₹4,000. The net profit as per Profit and Loss Appropriation Account will be :

(A) ₹3,54,000 (B) ₹3,46,000
(C) ₹4,09,000 (D) ₹4,01,000

42. *A* and *B* are partners. According to Profit and Loss Account, the net profit for the year is ₹2,00,000. The total interest on partner's drawings is ₹1,000. *A*'s salary is ₹40,000 per year and *B*'s salary is ₹3,000 per month. The net profit as per Profit and Loss Appropriation Account will be :

(A) ₹1,23,000 (B) ₹1,25,000
(C) ₹1,56,000 (D) ₹1,58,000

43. According to Profit and Loss Account, the net profit for the year is ₹1,40,000. The total interest on partner's capital is ₹8,000 and a partner is to be allowed commission of ₹5,000. The total interest on partner's drawings is ₹1,200. The net profit as per Profit and Loss Appropriation Account will be :
(A) ₹1,28,200 (B) ₹1,44,200
(C) ₹1,25,800 (D) ₹1,41,800

44. Mohit and Rohit were partners in a firm with capitals of ₹80,000 and ₹40,000 respectively. The firm earned a profit of ₹30,000 during the year. Mohit's share in the profit will be :
(A) ₹20,000 (B) ₹15,000
(C) ₹10,000 (D) ₹18,000
(C.B.S.E. 2020, Kerala)

45. *A*, *B* and *C* are partners. *A*'s capital is ₹3,00,000 and *B*'s capital is ₹1,00,000. *C* has not invested any amount as capital but he alone manages the whole business. *C* wants ₹30,000 p.a. as salary. Firm earned a profit of ₹1,50,000. How much will be each partner's share of profit :
(A) *A* ₹60,000; *B* ₹60,000; *C* ₹Nil
(B) *A* ₹90,000; *B* ₹30,000; *C* ₹Nil
(C) *A* ₹40,000; *B* ₹40,000 and *C* ₹40,000
(D) *A* ₹50,000; *B* ₹50,000 and *C* ₹50,000.

46. Net profit of a firm is ₹49,500. Manager is entitled to a commission of 10% on profits before charging his commission. Manager's Commission will be :
(A) ₹4,950 (B) ₹4,500
(C) ₹5,500 (D) ₹495

47. Net profit of a firm is ₹79,800. Manager is entitled to a commission of 5% of profits after charging his commission. Manager's Commission will be :
(A) ₹4,200 (B) ₹380
(C) ₹3,990 (D) ₹3,800

48. Ram and Shyam are partners in the ratio of 3 : 2. Before profit distribution, Ram is entitled to 5% commission of the net profit (after charging such commission). Before charging commission, firm's profit was ₹42,000. Shyam's share in profit will be :
(A) ₹16,000 (B) ₹24,000
(C) ₹26,000 (D) ₹16,400

49. *A*, *B* and *C* are partners in the ratio of 5 : 3 : 2. Before *B*'s salary of ₹17,000 firm's profit is ₹97,000. How much in total *B* will receive from the firm?
(A) ₹17,000 (B) ₹40,000
(C) ₹24,000 (D) ₹41,000

Hint : Total amount received by the partner will be Salary + Share of Profit

HOTS

50. *A*, *B* and *C* are partners in a firm without any agreement. They have

contributed ₹50,000, ₹30,000 and ₹20,000 by way of capital in the firm. *A* was unable to work for six months in a year due to illness. At the end of year, firm earned a profit of ₹15,000. *A*'s share in the profit will be :

(A) ₹7,500 (B) ₹3,750
(C) ₹5,000 (D) ₹2,500

HOTS

51. In a partnership firm, partner *A* is entitled a monthly salary of ₹7,500. At the end of the year, firm earned a profit of ₹75,000 after charging *A*'s salary. If the manager is entitled a commission of 10% on the net profit after charging his commission, Manager's commission will be :

(A) ₹7,500 (B) ₹16,500
(C) ₹8,250 (D) ₹15,000

52. Seeta and Geeta are partners sharing profits and losses in the ratio 4 : 1. Meeta was manager who received the salary of ₹4,000 p.m. in addition to a commission of 5% on net profits after charging such commission. Profit for the year is ₹6,78,000 before charging salary. Find the total remuneration of Meeta.

(A) ₹78,000 (B) ₹88,000
(C) ₹87,000 (D) ₹76,000

53. Which of the following statement is true?

(A) Fixed capital account will always have a credit balance
(B) Current account can have a positive or a negative balance
(C) Fluctuating capital account can have a positive or a negative balance
(D) All of the above

54. Abhay and Baldwin are partners sharing profit in the ratio 3 :1. On 31st March 2021, firm's net profit is ₹1,25,000. The partnership deed provided interest on capital to Abhay and Baldwin ₹15,000 and ₹10,000 respectively and Interest on drawings for the year amounted to ₹6,000 from Abhay and ₹4,000 from Baldwin. Abhay is also entitled to commission @10% on divisible profits. Calculate profit to be transferred to Partner's Capital A/c's.

(A) ₹1,00,000 (B) ₹1,10,000
(C) ₹1,07,000 (D) ₹ 90,000

(C.B.S.E. Sample Paper, 2021)

(iv) Capital Accounts of Partners

55. Which accounts are opened when the capitals are fixed?

(A) Only Capital Accounts
(B) Only Current Accounts
(C) Capital Accounts as well as Current Accounts
(D) Either Capital Accounts or Current Accounts

56. Which accounts are opened when the capitals are fluctuating?

(A) Only Capital Accounts
(B) Only Current Accounts

(C) Capital Accounts as well as Current Accounts
(D) Either Capital Accounts or Current Accounts

57. Balance of partner's current accounts are :
(A) Debit balance
(B) Credit balances
(C) Debit or Credit balances
(D) Neither Debit nor credit balances

58. Which item is recorded on the credit side of partner's current accounts :
(A) Interest on Partner's Capitals
(B) Salaries of Partners
(C) Share of profits of Partners
(D) All of the Above

59. If the Partners' Capital Accounts are fixed 'salary payable to partner' will be recorded :
(A) On the debit side of Partners' Current Account
(B) On the debit side of Partners' Capital Account
(C) On the credit side of Partners' Current Account
(D) None of the above

60. Which of the following is true regarding Salary to a partner when the firm maintains fluctuating capital accounts?
(A) Debit Partner's Loan A/c and Credit P & L Appropriation A/c.
(B) Debit P & L A/c and Credit Partner's Capital A/c.
(C) Debit P & L Appropriation A/c and Credit Partner's Current A/c.
(D) Debit P & L Appropriation A/c and Credit Partner's Capital A/c.
(C.B.S.E. Sample Paper, 2021)

61. It the Partner's Capital Accounts are fixed, interest on capital will be recorded:
(A) On the credit side of Current Account
(B) On the credit side of Capital Account
(C) On the debit side of Current Account
(D) On the debit side of Capital Account

62. If the Partner's Capital Accounts are fluctuating, in that case following item/items will be recorded in the credit side of capital accounts :
(A) Interest on capital
(B) Salary of partners
(C) Commission of partners
(D) All of the above

63. Interest on partner's capitals will be debited to :
(A) Profit and Loss Account
(B) Profit and Loss Appropriation Account
(C) Partner's Capital Accounts
(D) None of the Above

64. Interest on partner's capitals will be credited to :
(A) Profit and Loss Account
(B) Profit and Loss Appropriation Account
(C) Interest Account
(D) Partner's Capital Accounts

65. For the firm interest on drawings is
    (A) Capital Payment (B) Expenses
    (C) Capital Receipt (D) Income

66. Interest on Partner's drawings will be debited to :
    (A) Profit and Loss Account
    (B) Profit and Loss Appropriation Account
    (C) Partner's Current Account
    (D) Interest Account

67. When partners' capital accounts are floating, which one of the following items will be written on the credit side of the partners' capital accounts?
    (A) Interest on drawings
    (B) Loan advanced by partner to the firm
    (C) Partner's share in the firm's loss
    (D) Salary to the active partners

68. When partners' capital accounts are fixed, which one of the following items will be written in the partner's capital account?
    (A) Partner's Drawings
    (B) Additional capital introduced by the partner in the firm
    (C) Loan taken by partner from the firm
    (D) Loan Advanced by partner to the firm

69. Interest on partner's drawings will be credited to
    (A) Profit and Loss Account
    (B) Profit and Loss Appropriation Account
    (C) Partner's Capital Accounts
    (D) None of the Above

70. For the firm interest on capital is :
    (A) Capital Payment (B) Capital Receipt
    (C) Loss (D) Income

(v) Interest on Capital

71. On 1st April 2018, *X*'s Capital was ₹2,00,000. On 1st October 2018, he introduces additional capital of ₹1,00,000. Interest on capital @ 6% p.a. on 31st March, 2019 will be :
    (A) ₹9,000 (B) ₹18,000
    (C) ₹10,500 (D) ₹15,000

72. *X* and *Y* are partners in the ratio of 3 : 2. Their capitals are ₹2,00,000 and ₹1,00,000 respectively. Interest on capitals is allowed @ 8% p.a. Firm earned a profit of ₹60,000 for the year ended 31st March 2019. Interest on Capital will be :
    (A) *X* ₹16,000; *Y* ₹8,000 (B) *X* ₹8,000; *Y* ₹4,000
    (C) *X* ₹14,400; *Y* ₹9,600 (D) No Interest will be allowed

HOTS

73. Vidit and Seema were partners in a firm sharing profits and losses in the ratio of 3 : 2. Their capitals were ₹1,20,000 and ₹2,40,000, respectively. They were entitled to interest on capitals @ 10% p.a. The firm earned a profit of ₹18,000 during the year. The interest on Vidit's capital will be :

(A) ₹12,000 (B) ₹10,800
(C) ₹ 7,200 (D) ₹ 6,000

(C.B.S.E. 2020; Kolkata, Lucknow)

74. *X* and *Y* are partners in the ratio of 3 : 2. Their capitals are ₹2,00,000 and ₹1,00,000 respectively. Interest on capitals is allowed @ 8% p.a. Firm earned a profit of ₹15,000 for the year ended 31st March 2019. Interest on Capital will be :

(A) *X* ₹16,000; *Y* ₹8,000 (B) *X* ₹9,000; *Y* ₹6,000
(C) *X* ₹10,000; *Y* ₹5,000 (D) No Interest will be allowed

75. Mickey, Tom and Jerry were partners in the ratio of 5 :3 :2. On 31st March 2021, their books reflected a net profit of ₹2,10,000. As per the terms of the partnership deed they were entitled for interest on capital which amounted to ₹80,000, ₹60,000 and ₹40,000 respectively. Besides this a salary of ₹60,000 each was payable to Mickey and Tom.

Calculate the ratio in which the profits would be appropriated.

(A) 1 :1 :1 (B) 5 :3 :2
(C) 7 :6 :2 (D) 4 :3 :2

(C.B.S.E. Sample Paper, 2021)

HOTS

76. *X* and *Y* are partners in the ratio of 3 : 2. Their capitals are ₹2,00,000 and ₹1,00,000 respectively. Interest on capitals is allowed @ 8% p.a. Firm incurred a loss of ₹60,000 for the year ended 31st March 2019. Interest on Capital will be :

(A) *X* ₹16,000; *Y* ₹8,000 (B) *X* ₹8,000; *Y* ₹4,000
(C) *X* ₹14,400; *Y* ₹9,600 (D) No Interest will be allowed

HOTS

77. *X* and *Y* are partners in the ratio of 3 : 2. Their capitals are ₹2,00,000 and ₹1,00,000 respectively. Interest on capitals is allowed @ 8% p.a. Firm earned a profit of ₹15,000 for the year ended 31st March 2019. As per partnership agreement, interest on capital is treated a charge on profits. Interest on Capital will be :

(A) *X* ₹16,000; *Y* ₹8,000 (B) *X* ₹9,000; *Y* ₹6,000
(C) *X* ₹10,000; *Y* ₹5,000 (D) No Interest will be allowed

HOTS

78. *A* and *B* contribute ₹1,00,000 and ₹60,000 respectively in a partnership firm by way of capital on which they agree to allow interest @ 8% p.a. Their profit or loss sharing ratio is 3 : 2. The profit at the end of the year was ₹2,800 before allowing interest on capital. If there is a clear agreement that interest on

capital will be paid even in case of loss, then *B*'s share will be:

(A) Profit ₹6,000 (B) Profit ₹4,000
(C) Loss ₹6,000 (D) Loss ₹4,000

(vi) Interest on Drawings

HOTS

79. Partners are suppose to pay interest on drawing only when .... by the ....

(A) Provided, Agreement (B) Permitted, Investors
(C) Agreed, Partners (D) 'A' & 'C' above

HOTS

80. Where will you record interest on drawings :

(A) Debit Side of Profit & Loss Appropriation Account
(B) Credit Side of Profit & Loss Appropriation Account
(C) Credit Side of Profit & Loss Account
(D) Debit Side of Capital/Current Account only.

81. How would you close the Partner's Drawing Account :

(A) By transfer to Capital or Current Account Debit Side.
(B) By transfer to Capital Account Credit Side.
(C) By transfer to Current Account Credit Side.
(D) Either 'B' or 'C'.

82. If date of drawings of the partner's is not given in the question, interest is charged for how much time

(A) 1 month (B) 3 months
(C) 6 months (D) 12 months

83. Vikas is a partner in a firm. His drawings during the year ended 31st March, 2021 were ₹72,000. If interest on drawings is charged @ 9% p.a. the interest charged will be :

(A) ₹ 324 (B) ₹6,480
(C) ₹3,240 (D) ₹ 648

84. If a fixed amount is withdrawn by a partner on the first day of every month, interest on the total amount is charged for .... months.

(A) 6 (B) 6½
(C) 5½ (D) 12

85. If a fixed amount is withdrawn by a partner on the last day of every month, interest on the total amount is charged for .... months.

(A) 12 (B) 6½
(C) 5½ (D) 6

86. If a fixed amount is withdrawn by a partner in the middle of every month, interest on the total amount is charged for .... months.

(A) 6 (B) 6½
(C) 5½ (D) 12

87. In a partnership firm, a partner withdrew ₹5,000 per month on the first day of every month during the year for personal expenses. If interest on drawings is charged @ 6% p.a. the interest charged will be :
(A) ₹3,600 (B) ₹1,950
(C) ₹1,800 (D) ₹1,650

88. Ajay is a partner in a firm. He withdrew ₹2,000 per month on the last day of every month during the year ended 31st March, 2021. If interest on drawings is charged @ 9% p.a. the interest charged will be :
(A) ₹ 990 (B) ₹1,080
(C) ₹1,170 (D) ₹2,160

89. Sushil is a partner in a firm. He withdrew ₹4,000 per month in the middle of every month during the year ended 31st March, 2021. If interest on drawings is charged @ 8% p.a. the interest charged will be :
(A) ₹2,080 (B) ₹1,760
(C) ₹3,840 (D) ₹1,920

90. If fixed amount is withdrawn by a partner on the first day of each quarter, interest on the total amount is charged for .... months.
(A) 4.5 (B) 6
(C) 7.5 (D) 3

91. If a fixed amount is withdrawn by a partner on the last day of each quarter, interest on the total amount is charged for .... months.
(A) 6 (B) 4.5
(C) 7.5 (D) 3

92. If a fixed amount is withdrawn by a partner in each quarter, interest on the total amount is charged for .... months.
(A) 3 (B) 6
(C) 4.5 (D) 7.5

93. Anuradha is a partner in a firm. She withdrew ₹6,000 in the beginning of each quarter during the year ended 31st March, 2021. Interest on her drawings @ 10% p.a. will be :
(A) ₹ 900 (B) ₹1,200
(C) ₹1,500 (D) ₹ 600

94. Bipasa is a partner in a firm. She withdrew ₹6,000 at the end of each quarter during the year ended 31st March, 2021. Interest on her drawings @ 10% p.a. will be :
(A) ₹ 900 (B) ₹ 600
(C) ₹1,500 (D) ₹1,200

95. Charulata is a partner in a firm. She withdrew ₹10,000 in each quarter during the year ended 31st March, 2021. Interest on her drawings @ 9% p.a. will be:
(A) ₹1,350 (B) ₹2,250
(C) ₹ 900 (D) ₹1,800

HOTS

96. If equal amount is withdrawn by a partner in the beginning of each month during a period of 6 months, interest on the total amount will be charged for .... months.

(A) 2.5 (B) 3

(C) 3.5 (D) 6

97. If equal amount is withdrawn by a partner in the end of each month during a period of 6 months ending 31st March, 2021, interest on the total amount will be charged for .... months.

(A) 2.5 (B) 3

(C) 3.5 (D) 6

98. If equal amount is withdrawn by a partner in each month during a period of 6 months ending 31st March, 2021, interest on the total amount will be charged for .... months.

(A) 6 (B) 3

(C) 2.5 (D) 3.5

99. *X* is a partner in a firm. He withdrew regularly ₹1,000 at the beginning of every month for the six months ending 31st March, 2021. If interest on drawings is charged @ 8% p.a. the interest charged will be :

(A) ₹240 (B) ₹140

(C) ₹100 (D) ₹120

HOTS

100. *Y* is a partner in a firm. He withdrew regularly ₹3,000 at the end of every month for the six months ending 31st March, 2021. If interest on drawings is charged @ 10% p.a. the interest charged will be :

(A) ₹375 (B) ₹450

(C) ₹525 (D) ₹900

101. *Z* is a partner in a firm. He withdrew regularly ₹2,000 every month for the six months ending 31st March, 2021. If interest on drawings is charged @ 8% p.a. the interest charged will be :

(A) ₹480 (B) ₹280

(C) ₹200 (D) ₹240

102. A partner withdraws ₹8,000 each on 1st April and 1st Oct. Interest on his drawings @ 6% p.a. on 31st March will be :

(A) ₹480 (B) ₹720

(C) ₹240 (D) ₹960

103. A partner draws ₹2,000 each on 1st April 2020, 1st July 2020, 1st October, 2020 and 1st January 2021. For the year ended 31st March, 2021 interest on drawings @ 8% per annum will be :

(A) ₹540 (B) ₹320

(C) ₹960 (D) ₹400

104. A partner withdraws from firm ₹7,000 at the end of each month. At the rate of 6% per annum total interest will be :

(A) ₹5,040
(B) ₹2,310
(C) ₹3,570
(D) ₹1,370

(vii) Adjustments in the Closed Accounts

105. Anu and Tanu are equal partners with fixed capitals of ₹2,00,000 and ₹1,00,000 respectively. After closing the accounts for the year ending 31st March, 2021 it was discovered that interest on capitals @ 8% p.a. was omitted to be provided. In the adjusting entry :
(A) Anu will be credited by ₹16,000 and Tanu will be credited by ₹8,000
(B) Anu will be debited by ₹16,000 and Tanu will be debited by ₹8,000
(C) Anu will be credited by ₹4,000 and Tanu will be debited by ₹4,000
(D) Anu will be debited by ₹4,000 and Tanu will be credited by ₹4,000

106. Sony and Romy are equal partners with fixed capitals of ₹4,00,000 and ₹3,00,000 respectively. After closing the accounts for the year ending 31st March, 2021 it was discovered that interest on capitals was provided @ 8% instead of 10% p.a. In the adjusting entry :
(A) Sony will be credited by ₹8,000 and Romy will be credited by ₹6,000.
(B) Sony will be debited by ₹8,000 and Romy will be debited by ₹6,000.
(C) Sony will be debited by ₹1,000 and Romy will be credited by ₹1,000.
(D) Sony will be credited by ₹1,000 and Romy will be debited by ₹1,000.

107. Asha and Vipasha are equal partners with fixed capitals of ₹5,00,000 and ₹2,00,000 respectively. After closing the accounts for the year ending 31st March, 2021 it was discovered that interest on capitals was provided @ 6% instead of 5% p.a. In the adjusting entry :
(A) Asha will be debited by ₹1,500 and Vipasha will be credited by ₹1,500;
(B) Asha will be credited by ₹1,500 and Vipasha will be debited by ₹1,500;
(C) Asha will be debited by ₹5,000 and Vipasha will be debited by ₹2,000;
(D) Asha will be credited by ₹5,000 and Vipasha will be credited by ₹2,000.

108. *P* and *Q* sharing profits in the ratio of 2 : 1 have fixed capitals of ₹90,000 and ₹60,000 respectively. After closing the accounts for the year ending 31st March, 2021 it was discovered that interest on capitals was provided @ 6% instead of 8% p.a. In the adjusting entry :
(A) *P* will be credited by ₹1,800 and *Q* will be credited by ₹1,200;
(B) *P* will be debited by ₹200 and *Q* will be credited by ₹200;
(C) *P* will be credited by ₹200 and *Q* will be debited by ₹200;
(D) *P* will be debited by ₹1,800 and *Q* will be debited by ₹1,200

109. *A* and *B* sharing profits in the ratio of 7 : 3 have fixed capitals of ₹2,00,000 and ₹1,00,000 respectively. After closing the accounts for the year ending 31st March, 2021 it was discovered that interest on capitals was provided @ 12% instead of 10% p.a. In the adjusting entry :
(A) *A* will be debited by ₹4,000 and *B* will be debited by ₹2,000;
(B) *A* will be credited by ₹4,000 and *B* will be credited by ₹2,000;
(C) *A* will be debited by ₹200 and *B* will be credited by ₹200;
(D) *A* will be credited by ₹200 and *B* will be debited by ₹200

110. *X* and *Y* are partners in the ratio of 3 : 2. Their fixed capitals are ₹2,00,000 and ₹1,00,000 respectively. After clsoing the accounts for the year ending 31st March, 2021, it was discovered that interest on capital was allowed @ 12% instead of 10% per annum. By how much amount *X* will be debited/credited in the adjustment entry :

(A) ₹600 (Debit) (B) ₹400 (Credit)
(C) ₹400 (Debit) (D) ₹600 (Credit)

111. *X*, *Y* and *Z* are equal partners with fixed capitals of ₹2,00,000, ₹3,00,000 and ₹4,00,000 respectively. After closing the accounts for the year ending 31st March, 2021 it was discovered that interest on capitals @ 8% p.a. was omitted to be provided. In the adjusting entry :

(A) Dr. *X* and Cr. *Y* by ₹8,000 (B) Cr. *X* and Dr. *Z* by ₹8,000
(C) Dr. *X* and Cr. *Z* by ₹8,000 (D) Cr. *X* and Dr. *Y* by ₹8,000

112. *P*, *Q* and *R* are equal partners with fixed capitals of ₹5,00,000, ₹4,00,000 and ₹3,00,000 respectively. After closing the accounts for the year ending 31st March, 2021 it was discovered that interest on capitals was provided @ 7% instead of 9% p.a. In the adjusting entry :

(A) *P* will be credited by ₹2,000 and *Q* will be debited by ₹2,000.
(B) *P* will be debited by ₹2,000 and *Q* will be credited by ₹2,000.
(C) *P* will be debited by ₹2,000 and *R* will be credited by ₹2,000.
(D) *P* will be credited by ₹2,000 and *R* will be debited by ₹2,000.

113. *X*, *Y* and *Z* are equal partners with fixed capitals of ₹5,00,000, ₹3,00,000 and ₹1,00,000 respectively. After closing the accounts for the year ending 31st March, 2021 it was discovered that interest on capitals was provided @ 6% instead of 5% p.a. In the adjusting entry :

(A) Dr. *X* and Cr. *Z* by ₹2,000 (B) Cr. *X* and Dr. *Z* by ₹2,000
(C) Dr. *X* and Cr. *Y* by ₹2,000 (D) Cr. *X* and Dr. *Y* by ₹2,000

114. *P*, *Q* and *R* sharing profits in the ratio of 2 : 1 : 1 have fixed capitals of ₹4,00,000, ₹3,00,000 and ₹2,00,000 respectively. After closing the accounts for the year ending 31st March, 2021 it was discovered that interest on capitals was provided @ 6% instead of 8% p.a. In the adjusting entry :

(A) Cr. *P* ₹1,000; Dr. *Q* ₹1,500 and Cr. *R* ₹500
(B) Dr. *P* ₹500; Cr. *Q* ₹1,500 and Dr. *R* ₹1,000
(C) Cr. *P* ₹500; Dr. *Q* ₹1,500 and Cr. *R* ₹1,000
(D) Dr. *P* ₹1,000; Cr. *Q* ₹1,500 and Dr. *R* ₹500

115. *A*, *B* and *C* sharing profits in the ratio of 2 : 2 : 1 have fixed capitals of ₹3,00,000, ₹2,00,000 and ₹1,00,000 respectively. After closing the accounts for the year ending 31st March, 2021 it was discovered that interest on capitals was provided @ 12% instead of 10% p.a. In the adjusting entry :

(A) Cr. *A* ₹1,200; Dr. *B* ₹800 and Dr. *C* ₹400
(B) Dr. *A* ₹1,200; Cr. *B* ₹800 and Cr. *C* ₹400
(C) Cr. *A* ₹800; Cr. *B* ₹400 and Dr. *C* ₹1,200
(D) Dr. *A* ₹800; Dr. *B* ₹400 and Cr. *C* ₹1,200

116. *X, Y* and *Z* are partners in the ratio of 4 : 3 : 2. Salary to *X* ₹15,000 and to *Z* ₹3,000 omitted and profits distributed. For rectification, now *X* will be credited :

(A) ₹15,000 (B) ₹1,000
(C) ₹12,000 (D) ₹7,000

117. Simi, Manu and Beena are partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1. The balances of their fixed capital accounts on 1st April, 2020, were: Simi ₹1,00,000, Manu ₹1,00,000 and Beena ₹80,000.

After the accounts for the year ended 31st March, 2021, were prepared, it was discovered that interest on capital @ 10% per annum had been credited to the partners' current accounts even though it was not provided in the partnership deed.

The error in Simi's capital account / current account will be rectified by:

(A) Debiting her capital account with ₹1,200
(B) Crediting her current account with ₹1,200
(C) Debiting her current account with ₹1,200
(D) Crediting her capital account with ₹1,200

(I.S.C. Sample Paper, 2021)

(vii) Guarantee of Profit to a Partner

118. When a partner is given guarantee by other partners, loss on such guarantee will be borne by :

(A) Partnership firm
(B) All the other partners
(C) Partners who give the guarantee
(D) Partner with highest profit sharing ratio.

119. Guarantee given to partner '*A*' by the other partners '*B & C*' means :

(A) In case of loss '*A*' will not contribute towards that loss.
(B) In case of insufficient profits '*A*' will receive only the minimum guarantee amount.
(C) In case of loss or insufficient profits '*A*' will withdraw the minimum guarantee amount.
(D) All of the above.

120. *P, Q* and *R* are partners in a firm in 3 : 2 : 1. *R* is guaranteed that he will get minimum of ₹20,000 as his share of profit every year. Firm's profit was ₹90,000. Partners will get :

(A) *P* ₹40,000; *Q* ₹30,000; *R* ₹20,000;
(B) *P* ₹42,500; *Q* ₹27,500; *R* ₹20,000;
(C) *P* ₹45,000; *Q* ₹30,000; *R* ₹15,000;
(D) *P* ₹42,000; *Q* ₹28,000; *R* ₹20,000;

121. *X, Y* and *Z* are partners in the ratio of 5 : 4 : 3. *X* has given to *Z* a guarantee of minimum ₹10,000 profit. For the year ending 31st March, 2021, firm's profit is ₹28,800. *X*'s share in profit will be :

(A) ₹9,200 (B) ₹ 9,600
(C) ₹7,200 (D) ₹12,000

HOTS

122. *E*, *F* and *G* share profits in the ratio of 4 : 3 : 2. *G* is given a guarantee that his share of profits will not be less than ₹75,000. Deficiency if any, would be borne by *E* and *F* equally Firm's profit was ₹2,70,000. *F*'s share of profit will be :
(A) ₹90,000 (B) ₹82,500
(C) ₹97,500 (D) ₹75,000

123. Arif, Ravi and Ben are partners in a firm sharing profits and losses in the ratio of 6:4:1. Arif guaranteed a minimum profit of ₹16,000 to Ben. The trading profit of the firm for the year ending 31st March, 2021, was ₹1,32,000.
Arif's share in the profits of the firm will be:
(A) ₹72,000 (B) ₹68,000
(C) ₹69,600 (D) ₹16,000
(I.S.C. Sample Paper, 2021)

HOTS

124. *P*, *Q* and *R* are partners in 3 : 2 : 1. *R* is guaranteed that his share of profit will not be less than ₹70,000. Any deficiency will be borne by *P* and *Q* in the ratio of 2 : 1. Firm's profit was ₹2,40,000. Share of *P* will be :
(A) ₹1,00,000 (B) ₹1,10,000
(C) ₹1,20,000 (D) ₹1,02,000

125. *X*, *Y* and *Z* are partners in 5 : 4 : 1. *Z* is guaranteed that his share of profit will not be less than ₹80,000. Any deficiency will be borne by *X* and *Y* in 3 : 2. Firm's profit was ₹5,60,000. How much deficiency will be borne by *Y*?
(A) ₹2,14,400 (B) ₹14,400
(C) ₹2,09,600 (D) ₹ 9,600

HOTS

126. *P* and *Q* are partners sharing profits in the ratio of 1 : 2. *R* was manager who received the salary of ₹10,000 p.m. in addition to commission of 10% on net profits after charging such commission. Total remuneration to *R* amounted to ₹1,80,000. Profit for the year before charging salary and commission was :
(A) ₹7,20,000 (B) ₹6,00,000
(C) ₹7,80,000 (D) ₹6,60,000

HOTS

127. *A*, *B* and *C* are partners, their partnership deed provides for interest on drawings at 8% per annum. *B* withdrew a fixed amount in the middle of every month and his interest on drawings amounted to ₹4,800 at the end of the year. What was the amount of his monthly drawings?
(A) ₹ 10,000 (B) ₹ 5,000
(C) ₹1,20,000 (D) ₹48,000
(C.B.S.E. Sample Paper, 2021)

128. *X* and *Y* are partners. *X* draws a fixed amount at the beginning of every month. Interest on drawings is charged @8% p.a. At the end of the year interest on *X*'s drawings amounts to ₹2,600. Drawings of *X* were :

(A) ₹8,000 p.m. (B) ₹7,000 p.m.
(C) ₹6,000 p.m. (D) ₹5,000 p.m.

HOTS

129. *A* and *B* are partners. *B* draws a fixed amount at the end of every month. Interest on drawings is charged @15% p.a. At the end of the year interest on *B*'s drawings amounts to ₹8,250. Drawings of *B* were :

(A) ₹12,000 p.m. (B) ₹10,000 p.m.
(C) ₹ 9,000 p.m. (D) ₹ 8,000 p.m.

HOTS

130. *A* and *B* are partners with a profit sharing ratio of 2 : 1 and capitals of ₹3,00,000 and ₹2,00,000 respectively. They are allowed 6% p.a. interest on their capitals and are charged 10% p.a. interest on their drawings. Their drawings during the year were *A* ₹60,000 and *B* ₹40,000. *B*'s share of net profit as per profit and loss appropriation account amounted to ₹40,000. Net Profit of the firm before any appropriations was :

(A) ₹1,22,000 (B) ₹1,13,000
(C) ₹1,17,000 (D) ₹1,45,000

131. *A* and *B* are partners in a firm. They are entitled to interest on their capitals but the net profit was not sufficient for this interest, then the net profit will be distributed among partners in :

(A) Agreed Ratio (B) Profit Sharing Ratio
(C) Capital Ratio (D) Equally

132. *E*, *F* and *G* are partners sharing profits in the ratio of 3 : 3 : 2. As per the partnership agreement, *G* is to get a minimum amount of ₹80,000 as his share of profits every year and any deficiency on this account is to be personally borne by *E*. The net profit for the year ended 31st March, 2020 amounted to ₹3,12,000. Calculate the amount of deficiency to be borne by *E*?

(A) ₹1,000 (B) ₹4,000
(C) ₹8,000 (D) ₹2,000

(C.B.S.E. Sample Paper, 2020; 2021)

133. Pick the odd one out :

(A) Rent to Partner. (B) Manager's Commission.
(C) Interest on Partner's Loan. (D) Interest on Partner's Capital.

(C.B.S.E. Sample Paper, 2020)

134. Pick the odd one out from the following:

(A) Interest allowed on a loan taken by the firm from a partner
(B) Rent due to a partner of the firm for using his premises for business purposes

(C) Salary due to the manager of the firm

(D) Salary due to a partner of the firm *(I.S.C. Sample Paper, 2021)*

[See answers at the end of the book]

2

Goodwill : Concept and Valuation

Meaning of Goodwill :

Goodwill means the 'good-name' or the reputation earned by a firm through the hardwork and honesty of its owners. If a firm renders good service to the customers, the customers who feel satisfied will come again and again and the firm will be able to earn more profits in future.

Thus, goodwill is the value of the reputation of a firm which enables it to earn higher profits in comparison to the normal profits earned by other firms in the same trade.

Definitions :

"The term goodwill is generally used to denote the benefit arising from connections and reputation." — *Lord Lindley*

"Goodwill is nothing more than the probability that the old customers will resort to the old place." — *Lord Eldon*

"Goodwill may be said to be that element arising from the reputation, connections or other advantages possessed by a business which enables it to earn greater profits than the return normally to be expected on the capital represented by the net tangible assets employed in the business." — *Spicer and Pegler*

Characteristics or Features of Goodwill :

1. **It is an Intangible Asset :**— Goodwill belongs to the category of intangible assets such as patents, trade marks, copy rights etc. It does not suffer wear and tear and as such the question of depreciation does not arise on it, as is the case of other assets.
2. **It is a Valuable Asset.**
3. **It is Helpful in Earning Excess Profits.**
4. **Its Value is Liable to Constant Fluctuations :**— While goodwill does not depreciate, its value is liable to constant fluctuations. It is always present as a silent asset in a business where there are super profits (i.e., more than the normal) but declines in value with the decline in earnings.
5. **It is Valuable only when Entire Business is Sold :**— Goodwill cannot be sold in part. It can be sold with the entire business only. The only exception is at the time of admission and retirement of a partner.
6. **It is Difficult to Place an Exact Value on Goodwill :**— This is because its value may fluctuate from time to time due to changing circumstances which are internal and external to business.

Nature of Goodwill :

Goodwill is an intangible asset since it has no physical existence and cannot be seen or touched. But it is not a fictitious asset because fictitious assets do not have a value whereas goodwill has a value in case of profit making concerns. It can be sold, though a sale will be possible along with the sale of entire business.

Origin of Goodwill or Factors Affecting the Value of Goodwill

It is clear from the above, that the goodwill is the extra earning capacity of a business. Thus all factors which help a firm in earning profits affect the goodwill of the firm. Following factors affect the goodwill of a firm :

1. **Favourable Location of the Business :—** If the business is located at a convenient or prominent place, it will attract more customers and therefore will have more goodwill.

2. **Efficiency of Management :—** If the business is run by experienced and efficient management, its profits will go on increasing, which results in increase in the value of goodwill.

3. **The Longevity of the Business :—** An older business is better known to its customers, therefore it is likely to have more goodwill. When a business enterprise has built up good reputation over a period of time, the number of customers will be more in comparison to the customers of new entrants. Number of customers is an indicator of profit earning capacity of a business.

4. **Nature of Goods :—** If a business deals in goods of daily use, it will have steady profits as the demand for these goods will be stationary. Such business will have more goodwill. But if it deals in fancy goods, its profits will be uncertain and as such the value of the goodwill will be less.

5. **Possession of Licence :—** If a firm holds an import licence, the goodwill of the firm will be more as it will be very difficult for other firms to enter this business in the absence of this licence.

6. **Monopolistic and other Rights :—** If a business enjoys monopoly market, it will have assured profits. Similarly, if it holds some special rights such as patents, trade marks, copyrights or concessions, etc., it will have more goodwill.

7. **Risk Involved :—** If there is more risk involved in the business, the value of the goodwill will be less.

8. **Trend of Profit :—** If the profits of a business are increasing continuously, the value of its goodwill will be more. If the profits are declining or if the profits are uncertain, the value of its goodwill will be less.

9. **Future Competition :—** The likelihood or possibility of increased competition in future would definitely reduce the value of Goodwill.

10. **Capital Required :—** The amount of capital required for a business will also influence the value of goodwill. If two business enterprises earn the same rate of profit, the business with lesser capital requirement shall enjoy more goodwill.

11. **Other Factors :—**

(*i*) Good industrial relations

(*ii*) Favourable Government regulations

(*iii*) Stable political conditions
(*iv*) Research and development efforts
(*v*) Effective advertising to establish brand popularity
(*vi*) Popularity of product in terms of quality

Classification of Goodwill

Goodwill can be classified into two categories :

(1) Purchased Goodwill, and

(2) Self-Generated Goodwill or Inherent Goodwill

(1) **Purchased Goodwill** : Purchased goodwill is the goodwill which is acquired by making a payment. For example, when a business is purchased, the excess of purchase consideration over its net assets (*i.e.* Assets – Liabilities) is referred to as purchased goodwill.

The following are the **important features** of purchased goodwill :

(*i*) It arises on purchase of a business.
(*ii*) It is recorded in the books of accounts because consideration is paid for it.
(*iii*) It is shown in the Balance Sheet as an asset.
(*iv*) It is amortised at the earliest but not later than its useful economic life.

(2) **Self-Generated Goodwill or Inherent Goodwill** : It is internally generated goodwill which arises from a number of characteristics or attributes which an on-going business possesses.

The following are the **important features** of Self-Generated goodwill :

(*i*) It is internally generated over a long period of time.
(*ii*) A true cost cannot be placed on this type of goodwill. Its valuation depends on the subjective judgement of the valuer.
(*iii*) As per Accounting Standard 26 (Ind AS–38) (Intangible Assets), it is not recorded in the books of accounts because consideration in money or money's worth has not been paid for it.

**

Need for the Valuation of Goodwill

The need for valuing the goodwill in partnership arises in the following circumstances :

(1) On the admission of a new partner.
(2) On the retirement or death of a partner.
(3) When there is a change in the profit sharing ratio among the partners.
(4) If the goodwill is sold at the time of dissolution of the firm.
(5) When the firm is amalgamated with another firm.

Methods of Valuation of Goodwill

It is very difficult to assess the value of goodwill, as it is an intangible asset. In case of sale of a business, its value depends on the mutual agreement between the seller and the purchaser of the business. Following are the methods of valuing goodwill :

1. Average Profit Method

2. Super Profit Method
3. Capitalisation of Average Profit Method
4. Capitalisation of Super Profit Method

1. **Average Profit Method :—** This is a very simple and widely followed method of valuation of goodwill. In this method, goodwill is calculated on the basis of the number of past years profits. Average of such profits is multiplied by the agreed number of years (such as two or three) to find out the value of goodwill. Thus the formula is :

Value of Goodwill = Average Profit × Number of Years of Purchase

Why average profits? A buyer always wants to estimate the future profits of a business. Future profits depend upon the average performance of the business in the past. Past profits indicate as to what profits are likely to accrue in the future. Therefore the past profits are averaged. But before calculating the average profits, the profits earned in the past must be adjusted in the light of future expectations and the following factors should be taken into account while calculating the average profits :

(*i*) Abnormal income of a year should be deducted out of the net profit of that year.

(*ii*) Abnormal loss of a year should be added back to the net profit of that year.

(*iii*) Income from Investments should be deducted out of the net profits of that year, because this income is received from outside the business.

ILLUSTRATION 1.

Calculate goodwill of the firm on the basis of 3 year's purchase of the average profits of the last five years. The profits of the last five years were :

Year	*Amount (₹)*
2013-14	4,00,000
2014-15	5,00,000
2015-16	(60,000)
2016-17	1,50,000
2017-18	2,50,000

Additional Information :

(*i*) On 1st January, 2016, a fire broke out which resulted into a loss of goods of ₹3,00,000. A claim of ₹70,000 was received from the insurance company.

(*ii*) During the year ended 31st March, 2018 the firm received an unexpected tax refund of ₹80,000. (*C.B.S.E. 2019, Chennai*)

SOLUTION :

Total Profits of last 5 years :	₹
2013-14	4,00,000
2014-15	5,00,000
2015-16 (– ₹60,000 + Abnormal Loss ₹2,30,000)	1,70,000
2016-17	1,50,000
2017-18 (₹2,50,000 – Abnormal Gain ₹80,000)	1,70,000
	13,90,000

Average Profit = ₹13,90,000 ÷ 5 = ₹2,78,000

Goodwill = Average Profit × Number of Year's Purchase
= ₹2,78,000 × 3 = ₹8,34,000.

ILLUSTRATION 2.

A and *B* are partners sharing profits equally. They agree to admit *C* for equal share. For this purpose goodwill is to be valued at 150% of the average annual profits of the last 5 year's profits.

Profits were :

Year ended		₹
31st March	2015	40,000
,,	2016	60,000
,,	2017	1,00,000
,,	2018	20,000 (Loss)
,,	2019	1,50,000

It was observed that :

(1) During the year ended 31st March 2016, an asset of the original cost of ₹2,00,000 with book value of ₹1,50,000 was sold for ₹1,24,000.

(2) On 1st April, 2017, 2 Computer's costing ₹1,00,000 were purchased and were wrongly debited to Travelling Expenses. Depreciation on Computers was to be charged @ 20% p.a. on written down value basis.

Calculate the value of goodwill.

SOLUTION:

Calculation of Adjusted Profits

Particulars	2015	2016	2017	2018	2019
	₹	₹	₹	₹	₹
Profits	40,000	60,000	1,00,000	(20,000)	1,50,000
Add: Loss on Sale of Asset		26,000			
Add: Cost of Computers wrongly charged to P & L A/c				1,00,000	
Less: Depreciation on Computers				(20,000)$^{(1)}$	(16,000)$^{(2)}$
Adjusted Profits	40,000	86,000	1,00,000	60,000	1,34,000

$$\text{Average Profit} = \frac{40,000 + 86,000 + 1,00,000 + 60,000 + 1,34,000}{5}$$

$$= \frac{4,20,000}{5} = ₹84,000$$

$$\text{Value of Goodwill} = 84,000 \times \frac{150}{100} = ₹1,26,000$$

Working Note :

(1) Depreciation on Computers for the year ended 31.3.2018 = 20% on ₹1,00,000
= ₹20,000

(2) Depreciation on Computers for the year ended 31.3.2019 :
20% on (₹1,00,000 – ₹20,000) = ₹16,000

ILLUSTRATION 3.

A and *B* are partners in a firm sharing profits and losses in the ratio of 2 : 1. They decide to take *C* into partnership for 1/5th share on 1st April 2017. For this purpose goodwill is to be valued at 80% of the average annual profits of the previous three or four years, whichever is higher.

The profits for the last four years are :

	₹
Year ending on 31st March 2014	98,000
Year ending on 31st March 2015	80,000
Year ending on 31st March 2016	76,000
Year ending on 31st March 2017	1,20,000

Calculate the value of Goodwill.

SOLUTION :

Calculation of Average Profits

Based on 3 year's Profits	₹	*Based on 4 year's profits*	₹
31st March 2015	80,000	31st March 2014	98,000
31st March 2016	76,000	31st March 2015	80,000
31st March 2017	1,20,000	31st March 2016	76,000
		31st March 2017	1,20,000
	2,76,000		3,74,000
Average Profit = 2,76,000 ÷ 3 = ₹92,000		Average Profit = 3,74,000 ÷ 4 = ₹93,500	

4 year's average profit is higher than 3 year's average profit. Hence, the value of goodwill will be 80% of ₹93,500 = ₹74,800.

ILLUSTRATION 4.

A and *B* are partners sharing profits and losses in the ratio of 3 : 2. They agree to take *C* into partnership for 1/3rd share. For this purpose, goodwill is to be valued at two year's purchase of the average profit of last four years which were as follows :

	₹	
Year ending on 31st March 2014	50,000	(Profit)
Year ending on 31st March 2015	1,20,000	(Profit)
Year ending on 31st March 2016	1,80,000	(Profit)
Year ending on 31st March 2017	70,000	(Loss)

On 1st April, 2016 a Motor bike costing ₹50,000 was purchased and debited to travelling expenses account, on which depreciation is to be charged @ 20% p.a. calculate the value of goodwill.

SOLUTION :

Calculation of Average Profits :

	₹	
31st March 2014	50,000	(Profit)
31st March 2015	1,20,000	(Profit)
31st March 2016	1,80,000	(Profit)
31st March 2017	30,000[1]	(Loss)
	3,20,000	

Average Profit = ₹3,20,000 ÷ 4 = ₹80,000

Goodwill = Average Profit × Number of year's purchase
= ₹80,000 × 2 = ₹1,60,000.

Note :

(1) (*i*) Cost of Motor bike was wrongly debited to travelling expenses account. After rectification, the loss of 2017 will be reduced by ₹50,000.

(*ii*) Depreciation on Motor bike ₹10,000 (20% of 50,000) was not charged to Profit and Loss Account of 2017 which will increase the loss of 2017 by ₹10,000.

Hence, the final loss will be ₹70,000 – ₹50,000 + ₹10,000 = ₹30,000.

Weighted Average Profit Method :

This method is a modified version of average profit method. As per this method each year's profit is assigned a weight. The highest weight is attached to the profit of the most recent year. Thus, if profits are given for 2019, 2020, 2021 and 2022 and weighted average profit is to be calculated then weights will be assigned as follows :

2019 — 1; 2020 — 2; 2021 — 3; 2022 — 4.

Thereafter, each year's profit is multiplied by the weight assigned to it in order to find out the products and the total of products is then divided by the total of weights in order to calculate the weighted average profits. After this, the weighted average profit is multiplied by the agreed number of year's purchase to find out the value of goodwill. Thus, the formula is :

$$\text{Weighted Average Profit} = \frac{\text{Total of Products of Profits}}{\text{Total of Weights}}$$

Goodwill = Weighted Average Profit × Number of Year's of Purchase

Weighted average profit method is considered better than the simple average profit method because it assigns more weightage to the profits of the latest year which is more likely to be earned in the future. This method is preferred when the profits over the past four or five years have been continuously rising or falling.

ILLUSTRATION 5.

At the time of reconstitution of a partnership firm, goodwill was valued on the basis of three years' purchase of the weighted average profits of the last four years. The profits and losses of the preceding four years were :

Year	*Profits* (₹)	*Weights*
2013-14	22,000	1
2014-15	27,000	2
2015-16	32,000	3
2016-17	35,000	4

While valuing the goodwill of the firm it was found that the closing stock of the year 2015-16 was undervalued by ₹2,000.

You are required to calculate the value of goodwill on the date of reconstitution of the firm. *(ISC Sample Paper, 2018)*

SOLUTION :

Year	*Profits (₹)*	*Weights*	*Products*
2013-14	22,000	1	22,000
2014-15	27,000	2	54,000
2015-16	34,000 (Note 1)	3	1,02,000
2016-17	33,000 (Note 2)	4	1,32,000
		10	3,10,000

Weighted Average Profit $= \dfrac{3,10,000}{10} =$ ₹31,000

Goodwill at 3 year's purchase = ₹31,000 × 3 = ₹93,000

Notes : (1) Actual Profit for the year 2015-16 = ₹32,000
(+) Closing Stock Undervalued 2,000
34,000

(2) Actual Profit for the year 2016-17 = ₹35,000
(–) Opening Stock Undervalued 2,000
33,000

ILLUSTRATION 6.

It was agreed to calculate the value of goodwill of a firm at three years' purchase of the weighted average profits of the past four years. The appropriate weights to be used to each year ended on 31st March are: 2019—1; 2020—2; 2021—3; 2022—4.

The profits for these years ended on 31st March are : 2019 ₹20,200; 2020 ₹24,800; 2021 ₹20,000, and 2022 ₹30,000.

On a scrutiny of the accounts the following matters are revealed :—

(*i*) On 1st December, 2020 a major repair was made in respect of the plant incurring ₹6,000 which amount was charged to revenue. The paid sum is agreed to be capitalised for goodwill calculation subject to adjustment of depreciation of 10% p.a. on reducing balance method.

(*ii*) The closing stock for the year ending on 31st March 2020 was over-valued by ₹2,400.

(*iii*) To cover management cost an annual charge of ₹4,800 should be made for the purpose of goodwill valuation.

Compute the value of goodwill.

SOLUTION : CALCULATION OF ADJUSTED PROFITS

Year Ending	*31-3-2019*	*31-3-2020*	*31-3-2021*	*31-3-2022*
	₹	₹	₹	₹
Profits	20,200	24,800	20,000	30,000

Less : Charge for Management Cost	4,800	4,800	4,800	4,800
	15,400	20,000	15,200	25,200
Add : Capital expenditure charged to revenue	—	—	6,000	—
	15,400	20,000	21,200	25,200
Less : Depreciation (not provided)	—	—	200(1)	580(2)
	15,400	20,000	21,000	24,620
Less : Over Valuation of Closing Stock	—	2,400	—	—
	15,400	17,600	21,000	24,620
Add : Over Valuation of Opening Stock	—	—	2,400	—
	15,400	17,600	23,400	24,620

CALCULATION OF WEIGHTED AVERAGE PROFITS

Year Ending	*Profits* ₹	*Weight*	*Products*
31-3-2019	15,400	1	15,400
31-3-2020	17,600	2	35,200
31-3-2021	23,400	3	70,200
31-3-2022	24,620	4	98,480
		10	2,19,280

Weighted Average Profits $= \frac{2,19,280}{10} = 21,928$

Goodwill at 3 year's purchase $=$ ₹21,928 × 3 = ₹65,784

Working Notes :

(1) Depreciation for the year ending 31st March, 2021 = 10% of ₹6,000 for 4 months

$= 6,000 \times \frac{10}{100} \times \frac{4}{12} =$ ₹200.

(2) Depreciation for the year ending 31st March, 2022 = 10% of ₹5,800 (*i.e.*, 6,000 – 200)

$=$ ₹5,800 $\times \frac{10}{100} =$ ₹580

(3) Closing Stock of 2020 automatically becomes the Opening Stock of 2021.

ILLUSTRATION 7.

Calculate the goodwill of a firm on the basis of two year's purchase of the weighted average profits of the last five years. Weights assigned to each year would be: 1, 2, 3, 4 and 5 respectively to the profits ended 31st March 2015, 2016, 2017, 2018 and 2019.

The Profits for these five years were :

Year ended	*31st March, 2015*	*31st March, 2016*	*31st March, 2017*	*31st March, 2018*	*31st March, 2019*
Profits (₹)	36,000	1,70,000	1,90,000	2,00,000	3,50,000

Scrutiny of books of accounts revealed the following :

(*i*) An abnormal loss of ₹50,000 was incurred during the year ended 31st March, 2015.

(*ii*) An abnormal gain of ₹30,000 was earned during the year ended 31st March, 2016.

(*iii*) Repairs to Car amounting to ₹40,000 was wrongly debited to Vehicles A/c on 1st January, 2018. Depreciation was charged on Vehicles @ 10% p.a. on Straight Line Method.

(*iv*) Closing Stock as on 31st March 2018 was undervalued by ₹50,000.

SOLUTION : Calculation of Adjusted Profits

Particulars	*31st March, 2015*	*31st March, 2016*	*31st March, 2017*	*31st March, 2018*	*31st March, 2019*
	₹	₹	₹	₹	₹
Profits	36,000	1,70,000	1,90,000	2,00,000	3,50,000
Add : Abnormal Loss	50,000				
Less : Abnormal Gain		(30,000)			
Less : Repair expenses that should have been debited to P & L A/c				(40,000)	
Add : Depreciation wrongly debited to P & L A/c (There should have been no depreciation at all)				1,000$^{(1)}$	4,000$^{(2)}$
Add : Closing Stock under-valued				50,000$^{(3)}$	
Less : Opening Stock under-valued					(50,000)$^{(4)}$
Adjusted Profits	86,000	1,40,000	1,90,000	2,11,000	3,04,000

Calculation of Weighted Average Profits :

Year ended	*Profits* (₹)	*Weight*	*Products* (₹)
31.3.2015	86,000	1	86,000
31.3.2016	1,40,000	2	2,80,000
31.3.2017	1,90,000	3	5,70,000
31.3.2018	2,11,000	4	8,44,000
31.3.2019	3,04,000	5	15,20,000
		15	33,00,000

$$\text{Weighted Average Profit} = \frac{33{,}00{,}000}{15} = ₹2{,}20{,}000$$

Goodwill = Weighted Average Profit × Number of Year's Purchase
= ₹2,20,000 × 2 = ₹4,40,000

Working Notes :

1. Depreciation for the year ended 31.3.2018 :
10% on ₹40,000 for 3 months = ₹1,000.
2. Depreciation for the year ended 31.3.2019 :
10% on ₹40,000 (Under Straight Line Method) = ₹4,000.
3. Closing Stock under-valued reduced the profits of the year ended 31.3.2018. Hence, it is to be added to profits.
4. Closing Stock of previous year becomes Opening Stock of next year. Since Closing Stock of the year ended 31.3.2018 was undervalued, it means Opening Stock as on 1.4.2018 is also under-valued as a result of which profit for the year ended 31.3.2019 is higher by ₹50,000. Hence, profits will have to be reduced by this amount.

Limitations of Average Profit Method :

(*i*) **No Concrete Basis of Selecting the Number of Past Years :** There is no Concrete or genuine basis of selecting the number of past years on which average profit is to be calculated.

(*ii*) **Number of Years of Purchase of Profits are Based on Estimates :** In average profit method, average profits are multiplied by number of years (such as two or three) to find out the value of goodwill. However, the number of years of purchase used are based on estimation, hence, the value of goodwill cannot be stated as satisfactory. There should be some concrete or genuine basis for determining the number of years of purchase rather than based on estimates.

(*iii*) **Capital Employed is Ignored :** Capital employed is not considered while calculating average profits. Average profits earned by two firms engaged in the same type of business may be the same whereas capital employed by the two firms may be different. Hence, average profits cannot be the proper base for calculation of goodwill.

(*iv*) **Super Profits are Ignored :** If a firm is earning just the normal profits *i.e.*, if it is earning the same profits as the other firms in the same business, then the firm enjoys no goodwill. The firm can claim some value of goodwill only when it is earning super profit *i.e.*, it is earning more than what the other firms in the same business are earning. Hence, it is desirable to value goodwill on the basis of super profits and not the average profits.

2. **Super Profit Method :**— In this method goodwill is calculated on the basis of surplus (excess) profits earned by a firm in comparison to average profits earned by other firms. If a business has no anticipated excess earnings, it will have no goodwill. Such excess profits are called super profits and the goodwill is calculated on the basis of super profits. For example, if the normal rate of earning applicable in a particular type of business is 15% and if our firm is also engaged in the same type of business and we have invested ₹1,00,000 as capital and if we are earning ₹25,000 as profits, the Normal Profits at the rate of 15% on ₹1,00,000 should be ₹15,000, whereas, we are earning **Actual Profits** of ₹25,000. Therefore, ₹25,000 – ₹15,000 = ₹10,000 are **Super Profits.** Goodwill is calculated by multiplying the Super Profits by a reasonable number of years, such as two years purchase or three years purchase etc.

Thus the Formula is :

(i) Normal Profit $= \dfrac{\text{Capital Invested} \times \text{Normal Rate of Return}}{100}$

(ii) Super Profit = Actual or Average Profit – Normal Profit

(iii) Goodwill = Super Profit × No. of Years Purchased

ILLUSTRATION 8.

A firm earned net profits during the last seven years as follows :

2016	₹ 20,000 Profit	2020	₹2,70,000 Profit
2017	₹ 70,000 Loss	2021	₹3,00,000 Profit
2018	₹ 40,000 Loss	2022	₹3,20,000 Profit
2019	₹2,50,000 Profit		

The Capital invested in the firm is ₹12,00,000. Normal rate of return in the similar type of business is 10%. Calculate the value of goodwill on the basis of $2\frac{1}{2}$ years' purchases of average super profits earned during the above mentioned seven years.

SOLUTION :

(i) Actual Average Profit:

Total profits of last 7 years = ₹20,000 – ₹70,000 – ₹40,000 + ₹2,50,000 + ₹2,70,000 + ₹3,00,000 + ₹3,20,000
= ₹10,50,000

Average Profit $= \dfrac{10,50,000}{7}$ = ₹1,50,000

(ii) Normal Profit = Capital Invested × $\dfrac{\text{Normal Rate of Return}}{100}$

= 12,00,000 × $\dfrac{10}{100}$ = ₹1,20,000

(iii) Super Profit = Actual Average Profit – Normal Profit
= ₹1,50,000 – ₹1,20,000 = ₹30,000

(iv) Value of Goodwill = Super Profit × Number of Years Purchased
= ₹30,000 × 2.5 = ₹75,000.

ILLUSTRATION 9.

The average Net Profits expected in the future by *ABC* Firm are ₹36,000 per year. The average capital employed in the business by the firm is ₹2,00,000. The rate of return expected from capital invested in this class of business is 10%. The remuneration of the partners is estimated to be ₹6,000 per annum. Find out the value of goodwill on the basis of two years' purchase of Super Profits.

SOLUTION :

(i) Actual Average Profit : ₹36,000 – ₹6,000 = ₹30,000

(ii) Normal Profit = Capital Invested × $\dfrac{\text{Normal Rate of Return}}{100}$

= ₹2,00,000 × $\dfrac{10}{100}$ = ₹20,000

(*iii*) Super Profit = Actual Average Profit – Normal Profit
= ₹30,000 – ₹20,000 = ₹10,000

(*iv*) Value of Goodwill = Super Profit × No. of years' Purchased
= ₹10,000 × 2 = ₹20,000.

ILLUSTRATION 10.

Average profits of a firm during the last few years are ₹80,000 and the normal rate of return in a similar business is 10%. If the goodwill of the firm is ₹1,00,000 at 4 year's purchase of super profit, find the capital employed by the firm.

(C.B.S.E. 2019)

SOLUTION :

Goodwill = Super Profit × 4 Year's Purchase

₹1,00,000 = Super Profit × 4

Super Profit = $\frac{₹1,00,000}{4}$ = ₹25,000

Normal Profit = Actual Average Profit – Super Profit
= ₹80,000 – ₹25,000 = ₹55,000

Capital Employed = Normal Profit × $\frac{100}{\text{Normal Rate of Return}}$

= ₹55,000 × $\frac{100}{10}$ = ₹5,50,000

ILLUSTRATION 11.

Amit and Kartik are partners sharing profits and losses equally. They decided to admit Saurabh for an equal share in the profits. For this purpose the goodwill of the firm was to be valued at four years' purchase of super profits.

The Balance Sheet of the firm on Saurabh's admission was as follows :

Liabilities		*Amount*	*Assets*	*Amount*
		₹		₹
Capitals :			Machinery	75,000
Amit	90,000		Furniture	15,000
Kartik	50,000	1,40,000	Stock	30,000
Reserve		20,000	Sundry Debtors	20,000
Loan		25,000	Cash	50,000
Sundry Creditors		5,000		
		1,90,000		1,90,000

The normal rate of return is 12% per annum. Average profits of the firm for the last four years was ₹30,000. Calculate Saurabh's share of goodwill.

(C.B.S.E. 2018, Comptt.)

SOLUTION :

	₹
Capital Employed in the Firm :	
Amit's Capital	90,000

+	Kartik's Capital	50,000
+	Reserve	20,000
		1,60,000

Normal Profit $= \text{Capital Employed} \times \dfrac{\text{Normal Rate of Return}}{100}$

$= 1{,}60{,}000 \times \dfrac{12}{100} = ₹19{,}200$

Super Profit = Average Profit – Normal Profit

= ₹30,000 – ₹19,200 = ₹10,800

Goodwill = ₹10,800 × 4 = ₹43,200

Saurabh's Share of Goodwill = ₹43,200 × $\dfrac{1}{3}$ = ₹14,400.

ILLUSTRATION 12.

On April 1, 2020 an existing firm had assets of ₹75,000 including cash of ₹5,000. The partner's capital accounts showed a balance of ₹60,000 and reserve constituted the rest. If the normal rate of return is 10% and the goodwill of the firm is valued at ₹24,000 at 4 year's purchase of super profits, find the average profits of the firm.

SOLUTION :

Goodwill = Super Profits × 4 year's purchase

24,000 = Super Profits × 4

Super Profits = $\dfrac{24{,}000}{4}$ = ₹6,000

Normal Profits = Capital employed × $\dfrac{\text{Normal Rate of Return}}{100}$

= 75,000 × $\dfrac{10}{100}$ = ₹7,500

Super Profits = Average Profits – Normal Profits

Hence, Average Profits = Super Profits + Normal Profits

= ₹6,000 + ₹7,500 = ₹13,500.

ILLUSTRATION 13.

On 1st April, 2020, an existing firm had assets of ₹2,00,000 including cash of ₹4,000. Its creditors amounted to ₹10,000 on that date. The partner's capital accounts showed a balance of ₹1,60,000 while the general reserve amounted to ₹30,000. If the normal rate of return is 15% and the goodwill of the firm is valued at ₹36,000 at 3 year's purchase of super profit, find the average profits of the firm.

SOLUTION :

Goodwill = Super Profits × 3 Year's Purchase

36,000 = Super Profits × 3

Super Profits = $\dfrac{36{,}000}{3}$ = ₹12,000

Capital Employed = Assets – Creditors

= ₹2,00,000 – ₹10,000 = ₹1,90,000

OR

= Partner's Capital + General Reserve

= ₹1,60,000 + ₹30,000 = ₹1,90,000

Normal Profits = Capital Employed × $\frac{\text{Normal Rate of Return}}{100}$

= ₹1,90,000 × $\frac{15}{100}$ = ₹28,500

Super Profits = Average Profits – Normal Profits

Hence, Average Profits = Super Profits + Normal Profits

= ₹12,000 + ₹28,500 = ₹40,500

Difference between Average Profit and Super Profit

Basis	*Average Profit*	*Super Profit*
1. Meaning	It is average of the profits of past agreed years.	It is the excess of average profit over normal profit.
2. Normal Rate of Return	Normal rate of return is not considered for the calculation of average profit.	Normal rate of return is considered for the calculation of super profit.
3. Average Capital Employed	It is not considered while calculating the average profit.	It is considered while calculating the super profit.
4. Relevant for valuing goodwill	Average profit is required for valuing goodwill under all the three methods.	Super profit is required for valuing goodwill under Super Profit Method and Capitalisation of Super Profit Method only.

CASE BASED MCQs — 1

A, B and *C* were partners sharing profits in the ratio of 2 : 2 : 1. On this date firm had assets of ₹3,80,000 including cash of ₹20,000. The partner's capital accounts showed a balance of ₹3,00,000 and reserves constituted the rest. Normal rate of return is 10% and the goodwill of the firm is valued at ₹75,000 at 3 year's purchase of super profits.

On the basis of the above information, answer the following :

(*i*) Normal Profit of the firm is

(A) ₹30,000 (B) ₹38,000
(C) ₹36,000 (D) ₹40,000

(*ii*) Super Profit will be :

(A) ₹2,25,000 (B) ₹13,000
(C) ₹ 25,000 (D) ₹75,000

(*iii*) Average Profit will be :

(A) ₹13,000 (B) ₹38,000
(C) ₹25,000 (D) ₹63,000

CASE BASED MCQs — 2

P, *Q* and *R* are partners running a departmental store and sharing profits equally. They decided to value goodwill on the basis of 3 years purchase of super profits of last 5 years. Capital investment of the firm is ₹15,00,000 and a fair return on capital is 12% p.a. Profits of the last 5 years were as follows :

Year	*Profit* (₹)
Profit for the year ended 31st March 2016 :	1,60,000
Profit for the year ended 31st March 2017 :	(3,00,000)
Profit for the year ended 31st March 2018 : (including an abnormal gain of ₹60,000)	4,60,000
Profit for the year ended 31st March 2019 : (after charging an abnormal loss of ₹40,000)	4,00,000
Profit for the year ended 31st March 2020 :	3,00,000

On the basis of above information, answer the following :

(*i*) Average maintainable profit will be :

(A) ₹10,00,000 (B) ₹3,20,000
(C) ₹ 2,00,000 (D) ₹2,08,000

(*ii*) Normal profit of the firm is :

(A) ₹1,20,000 (B) ₹3,00,000
(C) ₹3,20,000 (D) ₹1,80,000

(*iii*) Value of goodwill of the firm will be :

(A) ₹60,000 (B) ₹84,000
(C) ₹80,000 (D) ₹20,000

3. Capitalisation Method : Under this method, goodwill can be calculated in two ways :

(*i*) By capitalising the average profits, or

(*ii*) By capitalising the super profits.

(*i*) Capitalisation of Average Profits Method : Under this method first of all we calculate the average profits and then we assess the capital needed for earning such average profits on the basis of normal rate of return. Such capital is also called capitalised value of average profits. It is calculated as under :

$$\text{Capitalised Value of Average Profits} = \text{Average Profits} \times \frac{100}{\text{Normal Rate of Return}}$$

If a firm earns a profit of ₹50,000 p.a. on an average basis and the normal rate of return is 10% p.a., the capitalised value of average profits will be :

$$50{,}000 \times \frac{100}{10} = ₹5{,}00{,}000$$

Goodwill is calculated by deducting the actual capital employed in business (*i.e.*, total tangible assets less outside liabilities on the date of valuation of Goodwill) from the capitalised value of average profits. If, in the above example, the actual capital employed amount to ₹4,00,000, the goodwill will be valued at ₹1,00,000, *i.e.*, ₹5,00,000 – ₹4,00,000. There will be no goodwill if the actual capital employed in the business exceeds or equals the capitalised value of average profits.

ILLUSTRATION 14.

From the figures given below, calculate goodwill according to the capitalisation of Average Profits Method :

(*i*)	Actual Average Profits	= ₹72,000
(*ii*)	Normal Rate of Return	= 10%
(*iii*)	Assets	= ₹9,70,000
(*iv*)	Liabilities	= ₹4,00,000

SOLUTION :

Capitalised Value of Average Profits $= \text{Average Profits} \times \dfrac{100}{\text{Normal Rate of Return}}$

$= 72{,}000 \times \dfrac{100}{10} = ₹7{,}20{,}000$

Capital Employed = Assets – Liabilities
(*i.e.*, Net Assets as on the date of Valuation of Goodwill)

= ₹9,70,000 – ₹4,00,000 = ₹5,70,000.

Goodwill = Capitalised Value of Average Profits – Net Assets
= ₹7,20,000 – ₹5,70,000 = ₹1,50,000.

ILLUSTRATION 15.

Varun and Kuber are partners in a business. Balance in Capital and Current Accounts on 31st March, 2019 were :

	Capital Account	*Current Account*
Varun	₹5,00,000	₹80,000
Kuber	₹3,50,000	₹20,000 (Dr.)

Profits of the last five consecutive years ending 31st March were : 2015 ₹60,000; 2016 Loss ₹40,000; 2017 ₹1,30,000; 2018 ₹2,00,000 and 2019 ₹2,50,000.

General Reserve appeared in the books at ₹50,000.

If the normal rate of return is 10%, find the value of goodwill by Capitalisation of Average Profit Method.

SOLUTION :

Average Profits $= \dfrac{60{,}000 - 40{,}000 + 1{,}30{,}000 + 2{,}00{,}000 + 2{,}50{,}000}{5} = ₹1{,}20{,}000$

Capitalised Value of Average Profits $= \text{Average Profit} \times \dfrac{100}{\text{Normal Rate of Return}}$

$= 1{,}20{,}000 \times \dfrac{100}{10} = ₹12{,}00{,}000$

Capital Employed = Capital Accounts + Current Accounts + General Reserve
= ₹5,00,000 + ₹3,50,000 + ₹80,000 – ₹20,000 + ₹50,000
= ₹9,60,000

Goodwill = Capitalised Value of Average Profits – Capital Employed
= ₹12,00,000 – ₹9,60,000 = ₹2,40,000.

(*ii*) **Capitalisation of Super Profit Method :** Under this method first of all we calculate the Super Profits and then we assess the capital needed for earning such super profits on the basis of normal rate of return. Such capital is actually the amount of goodwill. Following formula is used to calculate goodwill :

$$\text{Goodwill} = \text{Super Profit} \times \frac{100}{\text{Normal Rate of Return}}$$

Super Profits are calculated in the same manner as calculated in super profits method.

ILLUSTRATION 16.

From the figures given in Illustration 14, calculate goodwill according to the Capitalisation of Super Profit Method.

SOLUTION :

Capital Employed = Assets – Liabilities
= ₹9,70,000 – ₹4,00,000
= ₹5,70,000

Super Profit = Average Profit – Normal Profit
= ₹72,000 – ₹57,000 (10% of ₹5,70,000)
= ₹15,000

$$\text{Goodwill} = \text{Super Profit} \times \frac{100}{\text{Normal Rate of Return}}$$

$$= 15{,}000 \times \frac{100}{10} = ₹1{,}50{,}000.$$

ILLUSTRATION 17.

The following information relates to a partnership firm :

(*a*) Profits for the last five years :

2018	₹ 80,000	2019	₹1,00,000
2020	₹2,00,000	2021	₹1,50,000
2022	₹2,70,000		

(*b*) Average Capital Employed is ₹5,00,000.

(*c*) Rate of normal profit 20%.

Find out the value of goodwill on the basis of :

(*i*) Three year's purchase of average profits
(*ii*) Three year's purchase of super profits.
(*iii*) Capitalisation of super profits.

SOLUTION :

Average Profit :

Total Profits = ₹80,000 + ₹1,00,000 + ₹2,00,000 + ₹1,50,000 + ₹2,70,000
= ₹8,00,000

$$\text{Average Profit} = ₹\frac{8{,}00{,}000}{5} = ₹1{,}60{,}000$$

(*i*) On the basis of average profits :
Value of goodwill at 3 year's purchase of average profits :
₹1,60,000 × 3 = ₹4,80,000.

(*ii*) On the basis of super profits :

	₹
Average Profit	1,60,000
Less : Normal Profits 20% of ₹5,00,000	1,00,000
Super Profits	60,000

Value of goodwill at 3 year's purchase of super profits :
₹60,000 × 3 = ₹1,80,000.

(*iii*) On the basis of capitalisation of super profits :

$$\text{Goodwill} = \text{Super Profit} \times \frac{100}{\text{Normal Rate of Return}}$$

$$= ₹60{,}000 \times \frac{100}{20} = ₹3{,}00{,}000.$$

ILLUSTRATION 18.

From the following information, calculate goodwill of the firm of Anmol and Sujay at the time of admission of Dhruv :

(*i*) At three years' purchase of Super Profit.

(*ii*) On the basis of Capitalisation of Super Profit.

(*a*) Actual Average Profits of the firm for the last three years is ₹25,000.

(*b*) Normal Rate of Return is 10%.

(*c*) BALANCE SHEET OF ANMOL AND SUJAY
as at 31st March, 2019

Liabilities		₹	*Assets*	₹
Sundry Creditors		40,000	Plant and Machinery	40,000
Bills Payable		10,000	Land and Building	80,000
General Reserve		20,000	Investments (Non-trade)	50,000
Capital Accounts :			Sundry Debtors	15,000
Anmol	80,000		Bank	55,000
Sujay	90,000	1,70,000		
		2,40,000		2,40,000

(*I.S.C. 2020*)

SOLUTION :

(*i*) **On the basis of three year's Purchase of Super Profit :**

Capital Employed = Total Assets (excluding non-trade investments) – Outside Liabilities *i.e.* Creditors and B/P
= ₹2,40,000 – ₹50,000 – ₹40,000 – ₹10,000
= ₹1,40,000

$$\text{Normal Profit} = \text{Capital Employed} \times \frac{\text{Normal Rate of Return}}{100}$$

$$= 1{,}40{,}000 \times \frac{10}{100} = ₹14{,}000$$

Super Profit = Actual Average Profit – Normal Profit
= ₹25,000 – ₹14,000 = ₹11,000

Goodwill = Super Profit × Number of years Purchase
= ₹11,000 × 3 = ₹33,000.

(*ii*) **On the basis of Capitalisation of Super Profit :**

$$\text{Goodwill} = \text{Super Profit} \times \frac{100}{\text{Normal Rate of Return}}$$

$$= 11{,}000 \times \frac{100}{10} = ₹1{,}10{,}000.$$

SHORT ANSWER QUESTIONS

1. Define Goodwill.

2. Write any four factors which affect the goodwill of a partnership firm.

3. Why is 'Goodwill' considered an 'Intangible Asset' but not a 'Fictitious Asset'? *(I.S.C. 2020)*

Ans. Goodwill cannot be seen or touched, it can only be felt. Hence, it is treated as an intangible asset. But it is not a fictitious asset because fictitious assets do not have a value whereas goodwill has a value and it can be purchased or sold with any other asset.

4. On what occasions does the need for valuation of goodwill arise? *(I.S.C. 2019)*

Ans. On Admission of a partner.
On Retirement or Death of a partner.
On Change in Profit Sharing Ratio.
On Sale of the Firm.
On Amalgamation of two or more firms.
On Conversion of a partnership firm into a Company.

5. Explain any one method of goodwill valuation.

6. What is meant by 'Super Profit'? *(I.S.C. 2009)*

7. Distinguish between average profit and super profit method of valuation of goodwill.

8. What is meant by number of year's purchase in the valuation of a firm's goodwill? *(I.S.C. 2014)*

Ans. The buyer of a business will earn profits entirely due to seller's efforts for few years because buyer's efforts will start yielding profits after few years. Hence, the buyer should compensate the seller for few years future profits. Number of year's purchase means for how many years, the firm will earn the same amount of profit because of the past efforts.

9. Give the formula for valuation of goodwill by Capitalisation of Average Profit Method. *(I.S.C. 2018)*

Ans.

Goodwill = Capitalised Average Profit (–) Actual Capital Employed/net assets

Where, Capitalised Average Profit = Average Profit × $\frac{100}{\text{Normal Rate of Return}}$

Actual Capital Employed = Assets (excluding Goodwill and fictitious assets) *less* Outside Liabilities.

PRACTICAL QUESTIONS

(Question No. 1 to 16 are strictly in the serial order of Illustrations)

Valuation of Goodwill

Average Profit Method :

Q. 1. The goodwill of a firm is valued at 4 years' purchase of average profits of last five years. The profits of the last five years were :

Year		*Profit (₹)*
2017-18	:	2,00,000
2018-19	:	(3,00,000)
2019-20	:	4,50,000 (including an abnormal gain of ₹50,000)
2020-21	:	3,50,000 (after charging an abnormal loss of ₹90,000)
2021-22	:	2,60,000

Calculate the amount of goodwill.

[**Ans.** Goodwill ₹8,00,000]

Q. 2. *X* purchased the business of *Y* from 1st April, 2019. For this purpose goodwill is to be valued at 100% of the average annual profits of the last four years. The profits shown by *Y*'s business for the last four years were :

Year ended		(₹)	
31st March, 2016	Profit	1,00,000	(after debiting loss of stock by fire ₹50,000)
,, 2017	Loss	1,50,000	(includes voluntary retirement compensation paid ₹80,000)
,, 2018	Profit	1,50,000	
,, 2019	Profit	2,00,000	

Verification of books of accounts revealed the following :

(*i*) During the year ended 31st March, 2017, a machine got destroyed in accident and ₹60,000 was written off as loss in Profit & Loss Account.

(*ii*) On 1st July 2017, Two Computers costing ₹40,000 each were purchased and were debited to Travelling Expenses Account on which depreciation is to be charged @ 10% p.a. on Straight Line Method.

Calculate the value of goodwill.

[**Ans.** Goodwill ₹1,39,000.]

Hint. Profit for the year ended 31st March 2018 ₹2,24,000 and for 2019 ₹1,92,000.

Q. 3. *A*, *B* and *C* are partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. They decide to take *D* into partnership for 1/4th share on 1st April, 2022. For this purpose, goodwill is to be valued at 3 times the average annual profits of the previous four or five years whichever is higher. The agreed profits for goodwill

purpose of the past five years are as follows :

	₹
Year ending on 31st March 2018	1,30,000
Year ending on 31st March 2019	1,20,000
Year ending on 31st March 2020	1,50,000
Year ending on 31st March 2021	1,10,000
Year ending on 31st March 2022	2,00,000

Calculate the value of Goodwill.

[**Ans.** Goodwill ₹4,35,000]

Q. 4. *A, B* and *C* are partners sharing profits and losses equally. They agree to admit *D* for equal share. For this purpose goodwill is to be valued at 3 year's purchase of average profits of last 5 years which were as follows :

	₹	
Year ending on 31st March 2018	60,000	(Profit)
Year ending on 31st March 2019	1,50,000	(Profit)
Year ending on 31st March 2020	20,000	(Loss)
Year ending on 31st March 2021	2,00,000	(Profit)
Year ending on 31st March 2022	1,85,000	(Profit)

On 1st October, 2021 a computer costing ₹40,000 was purchased and debited to office expenses account on which depreciation is to be charged @25% p.a. Calculate the value of goodwill.

[**Ans.** Goodwill ₹3,66,000.]

Hint : Adjusted profit of 2017 will be : ₹1,85,000 + ₹40,000 – Depreciation ₹5,000 = ₹2,20,000.

Q. 5. The profits earned by a firm during the last four years were as follows :

Year ended 31st March	*Profits (₹)*
2019	80,000
2020	1,00,000
2021	1,10,000
2022	1,50,000

Calculate the value of goodwill on the basis of three year's purchase of weighted average profits. Weights to be used are 1, 2, 3 and 4 respectively to the profits for 2019, 2020, 2021 and 2022.

[**Ans.** Goodwill ₹3,63,000.]

Q. 6. Following information is available about the business of a firm :

(*i*) Profits : In 2020, ₹40,000; In 2021, ₹50,000; In 2022, ₹60,000, (*ii*) Non-recurring income of ₹1,000 is included in the profits of 2021, (*iii*) Profits of 2020 have been reduced by ₹6,000 because goods were destroyed by fire, (*iv*) Goods have not been insured but it is thought to insure them in future. The insurance premium is estimated at ₹400 per year, (*v*) Reasonable remuneration of the proprietor of business is ₹6,000 per year, but it has not been taken into account for calculation of above mentioned profits, (*vi*) Profits of 2022 include ₹5,000 income on investment.

Goodwill is agreed to be valued at two years' purchase of the weighted average profits of the past three years. The appropriate weights to be used are :—

2020 — 1; 2021 —2; 2022 —3.

[**Ans.** Value of Goodwill ₹90,200.]

Q. 7. Calculate the value of goodwill on the basis of three year's purchase of the weighted average profits of the last five years. Profits to be weighted 1, 2, 3, 4 and 5, the greatest weightage to be given to last year. Profits of the last five years were :

Year ended		(₹)	
31st March, 2015 :	Profit	80,000	
,, 2016 :	Profit	1,05,000	(after considering abnormal loss of ₹41,500)
,, 2017 :	Loss	20,000	(after considering abnormal gain of ₹40,000)
,, 2018 :	Profit	1,80,000	
,, 2019 :	Profit	2,00,000	

Books of Accounts of the firm revealed that :

(*i*) Closing Stock as on 31st March, 2015 was overvalued by ₹40,000.

(*ii*) Repairs to Machinery ₹60,000 were wrongly debited to Machinery Account on 1st July, 2017. Depreciation was charged on Machinery @ 20% p.a. on diminishing balance method.

[**Ans.** Value of Goodwill ₹3,60,000.]

Hint : Weighted Profit for the year ended 31st March 2018 ₹5,16,000 and 2019 ₹10,51,000.

Super Profit Method :

Q. 8. A partnership firm earned net profits during the last four years as follows :

Year	₹
1	56,000
2	64,000
3	60,000
4	62,000

The capital investment in the firm throughout the above mentioned period has been ₹3,00,000. Having regard to the risk involved, 15% is considered to be a fair return on the capital.

Calculate the value of goodwill on the basis of 3 years' purchase of average super profits earned during the above-mentioned four years.

[**Ans.** ₹46,500.]

Q. 9. The capital of the firm of Anuj and Benu is ₹10,00,000 and the market rate of interest is 15%. Annual salary to the partners is ₹60,000 each. The profit for the last three years were ₹2,80,000, ₹3,80,000 and ₹4,20,000. Goodwill of the firm is to be valued on the basis of two years purchase of last three years average super profits. Calculate the goodwill of the firm. *(C.B.S.E. 2019, M.P.)*

[**Ans.** Goodwill ₹1,80,000]

Q. 10. Find out the capital employed from the following information :

Normal rate of return :		12%
Profits : 2017-18	₹	80,000
2018-19	₹	1,30,000
2019-20	₹	1,56,000
Goodwill valued at 3 years purchase of Super Profits	₹	1,50,000

[**Ans.** Capital Employed ₹6,00,000]

Q. 11. *A* and *B* are partners. They admit *C* for $\frac{1}{4}$th share in profits. For this purpose goodwill is to be valued at three year's purchase of super profits.

Following information is provided to you :

	₹
A's Capital	5,00,000
B's Capital	4,00,000
General Reserve	1,50,000
Profit & Loss A/c (Cr.)	30,000
Sundry Assets	12,00,000

The normal rate of return is 15% p.a. Average Profits are ₹2,00,000 per year. You are required to calculate *C*'s share of goodwill.

[**Ans.** *C*'s share of goodwill ₹28,500.]

Hint. Sundry Assets will be ignored.

Q. 12. The net assets of a firm as on March 31, 2022 were ₹4,00,000. If the normal rate of return is 20% and the goodwill of the firm is valued at ₹1,25,000 at 5 year's purchase of super profits, find the average profits of the firm.

[**Ans.** Average Profit ₹1,05,000]

Q. 13. On April Ist 2022, an existing firm had assets of ₹5,00,000 including cash of ₹20,000. The firm had a General Reserve of ₹90,000, partner's capital accounts showed a balance of ₹3,80,000 and creditors amounted to ₹30,000. If the normal rate of return is 20% and the goodwill of the firm is valued at ₹64,000 at 4 year's purchase of super profit, find the average profits of the firm.

[**Ans.** ₹1,10,000]

Capitalisation Method :

Q. 14. The average profits of a firm is ₹48,000. The total assets of the firm are ₹8,00,000. Value of other liabilities is ₹5,00,000. Average rate of return in the same business is 12%.

Calculate goodwill from capitalisation of average profits method.

[**Ans.** ₹1,00,000.]

Hint : Capital Employed = Assets – Liabilities.

Q. 15. Anupma, Purnima and Ruchika are partners in a business. Balances in their Capital and Current Accounts as on 31st March, 2019 were :

	Capital Account (₹)	*Current Account* (₹)
Anupma	6,00,000	60,000 (Dr.)
Purnima	5,00,000	30,000 (Dr.)
Ruchika	5,00,000	10,000 (Cr.)

The firm earned an average profit of ₹2,40,000. If the normal rate of return is 12%, find the value of goodwill by Capitalisation of Average Profit Method.

[**Ans.** Value of Goodwill ₹4,80,000]

Q. 16. Calculate the value of goodwill according to capitalisation of Super Profits Method in the previous Q. 14.

[**Ans.** ₹1,00,000]

Q. 17. The following information relates to a partnership firm :

(*a*) Profits/Losses for the last six years :

1st year	₹20,000 Profit	4th year	₹60,000 Profit
2nd year	₹60,000 Profit	5th year	₹50,000 Profit
3rd year	₹10,000 Loss	6th year	₹72,000 Profit

(*b*) Average Capital Employed is ₹2,00,000.

(*c*) Rate of normal profit is 15%.

Find out the value of goodwill on the basis of :

(*i*) Four years' purchase of average profits.

(*ii*) Four years' purchase of super profits.

(*iii*) Capitalisation of super profits.

[**Ans.** (*i*) On the basis of average profits ₹1,68,000
(*ii*) On the basis of super profits ₹ 48,000
(*iii*) On the basis of capitalisation of super profits ₹ 80,000.]

ADDITIONAL QUESTIONS

Valuation of Goodwill

Q. 18. Calculate the value of goodwill as on 1st April, 2022, on the basis of $2\frac{1}{2}$ year's purchase of the average profits of the last five years. The profits and losses for the years ending 31st March were: 2017 ₹80,000; 2018 ₹1,00,000; 2019 Loss ₹30,000; 2020 ₹1,70,000; 2021 ₹1,60,000 and 2022 ₹1,80,000. You are informed that the profits of the year ending 31st March 2021 included profit on sale of a fixed asset amounting to ₹50,000 and the profits for the year 2022 were effected by a loss due to fire amounting to ₹20,000.

[**Ans.** ₹2,75,000.]

Hint. Profit for the year 2017 will be ignored.

Q. 19. Calculate the value of goodwill at 2 year's purchase of the average profits of the last 3 years. The profit for the first year was ₹50,000, for second year twice the profit of first year and for the third year one and half times the profit of the second year.

[**Ans.** ₹2,00,000]

Q. 20. *A* firm earned net profits during the last five years as follows :

I. ₹7,000; II. ₹6,500, III. ₹8,000; IV. ₹7,500; V. ₹6,000.

The capital investment of the firm is ₹40,000. A fair return on capital in the market is 12%. Find out the value of goodwill of the business if it is based on three year's purchase of average super profits of the past five years.

[**Ans.** Goodwill ₹6,600.]

Q. 21. A firm earns a profit of ₹37,000 per year. In the same business a 10% return is generally expected. The total assets of the firm are 4,00,000. The value of other liabilities is ₹90,000. Find out the value of goodwill.

[**Ans.** Goodwill ₹60,000.]

Q. 22. An existing firm had assets of ₹4,00,000 including cash of ₹15,000. The partner's capital accounts showed a balance of ₹3,00,000 and reserves constituted the rest. If the normal rate of return is 12% and the goodwill of the firm is valued at ₹50,000 at $2\frac{1}{2}$ year's purchase of super profits, find the average profits of the firm.

[**Ans.** ₹68,000]

Q. 23. An existing firm had assets of ₹4,00,000 including cash of ₹15,000. Its creditors amounted to ₹20,000 on that date. The partner's capital accounts showed a balance of ₹3,00,000 and reserves amounted to ₹80,000. If the normal rate of return is 10% and the goodwill of the firm is valued at ₹75,000 at 3 year's purchase of super profits, find the average profits of the firm.

[**Ans.** ₹63,000.]

Q. 24. Yash and Karan were partners in an interior designer firm. Their fixed capitals were ₹6,00,000 and ₹4,00,000 respectively. There were credit balances in their current accounts of ₹4,00,000 and ₹5,00,000 respectively. The firm had a balance of ₹1,00,000 in General Reserve. The firm did not have any liability. They admitted Radhika into partnership for 1/4th share in the profits of the firm. The average profits of the firm for the last five years were ₹5,00,000. Calculate the value of goodwill of the firm by capitalization of average profits method. The normal rate of return in the business is 10%. *(C.B.S.E. 2020, Lucknow, Kolkata)*

[**Ans.** Goodwill ₹30,00,000.]

Q. 25. A business has earned average profits of ₹1,00,000 during the last few years and the normal rate of return in similar business is 10%. Find out the value of Goodwill by :

(*i*) Capitalisation of super profit method and

(*ii*) Super profit method if the goodwill is valued at 3 years purchase of super profit.

The assets of the business were ₹10,00,000 and its external liabilities ₹1,80,000.

[**Ans.** (*i*) As per capitalisation of Super Profits ₹1,80,000; (*ii*) As per Super Profits ₹54,000.]

Q. 26. A Partnership firm earned net profits during the last three years as follows:

Years	*Net Profit* (₹)
2019-20	1,90,000
2020-21	2,20,000
2021-22	2,50,000

The capital employed in the firm throughout the above mentioned period has been ₹4,00,000. Having regard to the risk involved, 15% is considered to be a fair return on the capital. The remuneration of all the partners during this period is estimated to be ₹1,00,000 per annum.

Calculate the value of goodwill on the basis of (*i*) two year's purchase of super profits earned on average basis during the above mentioned three years and (*ii*) by capitalisation of average profits method.

[**Ans.** (*i*) As per Super Profits ₹1,20,000; (*ii*) As per Capitalisation of Average Profits ₹4,00,000.]

Q. 27. Average profit of the firm is ₹3,00,000. Total assets of the firm are ₹24,00,000 whereas Partner's Capital is ₹20,00,000. If normal rate of return in a similar business is 12% of the capital employed, what is the value of goodwill by Capitalisation of Super Profit?

[**Ans.** Value of Goodwill ₹5,00,000]

Q. 28. The following information relates to a partnership firm :

(*a*) Sundry Assets of the firm ₹6,80,000. Outside Liabilities ₹60,000.

(*b*) Profits and losses for the past years : Profit 2019 ₹50,000; Loss 2020 ₹10,000; Profit 2021 ₹1,64,000 and Profit 2022 ₹1,80,000.

(*c*) The normal rate of return in a similar type of business is 12%.

Calculate the value of goodwill on the basis of :

(*i*) Three year's purchase of average profits.

(*ii*) Three year's purchase of super profits.

(*iii*) Capitalisation of average profits, and

(*iv*) Capitalisation of super profits.

[**Ans.** (*i*) ₹2,88,000; (*ii*) ₹64,800; (*iii*) ₹1,80,000 and (*iv*) ₹1,80,000]

MULTIPLE CHOICE QUESTIONS

Choose the Best Alternative :

1. Which of the following is True in relation to goodwill?

(A) Goodwill is a fictitious asset
(B) Goodwill is a current asset
(C) Goodwill is a wasting asset
(D) Goodwill is an intangible asset

2. The excess amount which the firm can get on selling its assets over and above the saleable value of its assets is called :

(A) Surplus
(B) Super profits
(C) Reserve
(D) Goodwill

HOTS

3. Which of the following is NOT true in relation to goodwill?
   (A) It is an intangible asset
   (B) It is fictitious asset
   (C) It has a realisable value
   (D) None of the above

4. When Goodwill is not purchased goodwill account can :
   (A) Never be raised in the books
   (B) Be raised in the books
   (C) Be partially raised in the books
   (D) Be raised as per the agreement of the partners

HOTS

5. The Goodwill of the firm is NOT affected by :
   (A) Location of the firm
   (B) Reputation of firm
   (C) Better customer service
   (D) None of the above

6. Capital employed by a partnership firm is ₹5,00,000. Its average profit is ₹60,000. The normal rate of return in similar type of business is 10%. What is the amount of super profits?
   (A) ₹50,000
   (B) ₹10,000
   (C) ₹ 6,000
   (D) ₹56,000

7. Weighted average method of calculating goodwill is used when :
   (A) Profits are not equal
   (B) Profits show a trend
   (C) Profits are fluctuating
   (D) None of the above

8. The profits earned by a business over the last 5 years are as follows : ₹12,000; ₹13,000; ₹14,000; ₹18,000 and ₹2,000 (loss). Based on 2 years purchase of the last 5 years profits, value of Goodwill will be :
   (A) ₹ 23,600
   (B) ₹ 22,000
   (C) ₹1,10,000
   (D) ₹1,18,000

9. The average profit of a business over the last five years amounted to ₹60,000. The normal commercial yield on capital invested in such a business is deemed to be 10% p.a. The net capital invested in the business is ₹5,00,000. Amount of goodwill, if it is based on 3 years purchase of last 5 years super profits will be :
   (A) ₹1,00,000
   (B) ₹1,80,000
   (C) ₹ 30,000
   (D) ₹1,50,000

10. Tangible Assets of the firm are ₹14,00,000 and outside liabilities are ₹4,00,000. Profit of the firm is ₹1,50,000 and normal rate of return is 10%. The amount of Capital employed will be
    (A) ₹10,00,000
    (B) ₹1,00,000
    (C) ₹ 50,000
    (D) ₹ 20,000

(C.B.S.E. 2020; Punjab)

HOTS

11. Under the capitalisation method, the formula for calculating the goodwill is :
    (A) Super profits multiplied by the normal rate of return
    (B) Capital employed multiplied by the normal rate of return
    (C) Super profits divided by the normal rate of return
    (D) Capital employed divided by the normal rate of return
    (I.S.C. Sample Paper, 2021)

12. Total assets of a firm including fictitious assets of ₹5,000 are ₹85,000. The net liabilities of the firm are ₹30,000. The normal rate of return is 10% and the average profits of the firm are ₹8,000. Calculate the goodwill as per capitalisation of super profits.
    (A) ₹20,000 (B) ₹30,000
    (C) ₹25,000 (D) None of these

13. Total Capital employed in the firm is ₹8,00,000, reasonable rate of return is 15% and Profit for the year is ₹12,00,000. The value of goodwill of the firm as per capitalization method would be :
    (A) ₹82,00,000 (B) ₹12,00,000
    (C) ₹72,00,000 (D) ₹42,00,000

14. The average capital employed of a firm is ₹4,00,000 and the normal rate of return is 15%. The average profit of the firm is ₹80,000 per annum. If the remuneration of the partners is estimated to be ₹10,000 per annum, then on the basis of two years purchase of super-profit, the value of the Goodwill will be :
    (A) ₹10,000 (B) ₹20,000
    (C) ₹60,000 (D) ₹80,000

15. A firm earns ₹1,10,000. The normal rate of return is 10%. The assets of the firm amounted to ₹11,00,000 and liabilities to ₹1,00,000. Value of goodwill by capitalisation of Average Actual Profits will be :
    (A) ₹2,00,000 (B) ₹ 10,000
    (C) ₹ 5,000 (D) ₹1,00,000

16. Capital invested in a firm is ₹5,00,000. Normal rate of return is 10%. Average profits of the firm are ₹64,000 (after an abnormal loss of ₹4,000). Value of goodwill at four times the super profits will be :
    (A) ₹ 72,000 (B) ₹ 40,000
    (C) ₹2,40,000 (D) ₹1,80,000

[See answers at the end of the book]

3

Admission of a Partner

LEARNING OBJECTIVES

After studying this Chapter you should be able to understand :

- **New Profit Sharing Ratio**
- **Sacrificing Ratio**
- **Accounting Treatment of Goodwill when a new partner is admitted**
- **Accounting Treatment for Revaluation of Assets and Liabilities**
- **Accounting Treatment of Reserves and Accumulated Profits**
- **Adjustment of Capitals :**
  - **(*i*) Determining the New Partner's Capital on the basis of Combined Capital of Old Partners**
  - **(*ii*) Adjusting the Capitals of Old Partners on the basis of the Capital of New Partner**

Sometimes a new partner is needed into the business due to the following reasons :

1. When more capital is needed for the expansion of the business;
2. When a competent and experienced person is needed for the efficient running of the business;
3. To increase the goodwill and reputation of the business by taking a reputed and renowned person into the partnership;
4. To encourage a capable employee by taking him into the partnership.

A new partnership deed is prepared at the time of admission of a new partner, as the old partnership deed comes to an end. According to Section 31 (1) of the Indian Partnership Act, a new partner can be admitted only with the consent of all the existing partners.

Rights of a New Partner : A new partner gets the following two rights :

(1) Right to share future profits of the firm; and

(2) Right to share in the assets of the firm.

At the same time, he becomes liable for any liability incurred by the firm after his admission.

At the time of admission, the new partner brings his share of goodwill and capital.

Old partners sacrifice a share of their profits in his favour and thus he gets a share in the future profits of the firm. Following adjustments are needed at the time of the admission of a new partner :

1. Calculation of new profit sharing ratio;
2. Accounting treatment of Goodwill;
3. Accounting treatment of Joint Life Policy
4. Accounting treatment for revaluation of assets and liabilities;
5. Accounting treatment of reserves and accumulated profits;
6. Adjustment of Capitals on the basis of new profit sharing ratio.

Calculation of New Profit Sharing Ratio

When a new partner is admitted, he acquires his share of profit from the old partners. This reduces the old partners' shares of profits, hence the calculation of new profit sharing ratio becomes necessary.

Following types of problems may arise for the calculation of new profit sharing ratios, at the time of admission of a new partner :

(1) When only the ratio of the new partner is given in the question, then in the absence of any other agreement, it is presumed that the old partners will continue to share the remaining profits in the same ratio in which they were sharing before the admision of the new partner.

ILLUSTRATION 1.

(*a*) *A*, *B* and *C* are partners in proportion of $\frac{3}{6}$, $\frac{2}{6}$ and $\frac{1}{6}$ respectively. *D* was admitted in the firm as a new partner with $\frac{1}{6}$ th share. Calculate the new profit sharing ratios of the partners.

(*b*) *A*, *B* and *C* are partners sharing profits in the ratio of 5 : 4 : 3. *D* was admitted for 10% profits. Calculate the new profit sharing ratio.

SOLUTION :

(*a*) Calculation of new profit sharing ratios :

Let total profit be $= 1$

Share given to *D* $= \frac{1}{6}$

Remaining Share $= 1 - \frac{1}{6} = \frac{5}{6}$

Now the old partners will share this remaining profit in their old profit sharing ratios :

Hence,

A's Share $= \frac{3}{6}$ of $\frac{5}{6} = \frac{5}{12}$

B's Share $= \frac{2}{6}$ of $\frac{5}{6} = \frac{5}{18}$

C's Share $= \frac{1}{6}$ of $\frac{5}{6} = \frac{5}{36}$

D's Share $= \frac{1}{6}$

Thus, the new profit sharing ratio of *A, B, C* and *D* will be :

$$= \frac{5}{12} : \frac{5}{18} : \frac{5}{36} : \frac{1}{6} = \frac{15 : 10 : 5 : 6}{36} = 15 : 10 : 5 : 6$$

(*b*) D's Share $=$ 10% or $\frac{10}{100}$ or $\frac{1}{10}$th

Remaining share $= 1 - \frac{1}{10} = \frac{9}{10}$

A, B and *C* will share this remaining share in their old profit sharing ratio.

A's new share $= \frac{5}{12}$ of $\frac{9}{10} = \frac{15}{40}$

B's new share $= \frac{4}{12}$ of $\frac{9}{10} = \frac{12}{40}$

C's new share $= \frac{3}{12}$ of $\frac{9}{10} = \frac{9}{40}$

D's share $= \frac{1}{10}$

Thus, new profit sharing ratio of *A, B, C* and *D* =

$$\frac{15}{40} : \frac{12}{40} : \frac{9}{40} : \frac{1}{10} = \frac{15 : 12 : 9 : 4}{40} \text{ or } 15 : 12 : 9 : 4$$

(2) Sometimes the new partner 'purchases' his share of profit from the old partners equally. In such cases the new profit sharing ratios of the old partners will be ascertained by deducting the sacrifice made by them from their existing share of profit.

ILLUSTRATION 2.

(*a*) Ram and Shyam are partners sharing profits and losses in the ratio of $\frac{7}{12} : \frac{5}{12}$. They admit Gopi as a new partner for 1/6 th share, which he acquires equally from Ram and Shyam. Calculate the new profit sharing ratios of the partners.

(*b*) *A, B* and *C* were partners in a firm sharing profits in the ratio of 3 : 2 : 1. They admitted *D* as a new partner for 1/8th share in the profits, which he acquired 1/16th from *B* and 1/16th from *C*.

Calculate the new profit sharing ratio of *A, B, C* and *D*.

SOLUTION :

(*a*) Share of Profits given to Gopi $= \frac{1}{6}$

Share acquired by Gopi from Ram $= \frac{1}{2}$ of $\frac{1}{6} = \frac{1}{12}$

Share acquired by Gopi from Shyam $= \frac{1}{2}$ of $\frac{1}{6} = \frac{1}{12}$

Therefore,

Ram's new share after surrendering $\frac{1}{12}$ in Gopi's favour $= \frac{7}{12} - \frac{1}{12} = \frac{6}{12}$

Shyam's new share after surrendering $\frac{1}{12}$ in Gopi's favour $= \frac{5}{12} - \frac{1}{12} = \frac{4}{12}$

Gopi's Share $= \frac{1}{12} + \frac{1}{12} = \frac{1}{6}$

Hence, the new profit sharing ratio of Ram, Shyam and Gopi will be :

$$= \frac{6}{12} : \frac{4}{12} : \frac{1}{6} = \frac{6:4:2}{12} = 6:4:2 = 3:2:1$$

(*b*) *A*'s new Share $= \frac{3}{6}$ *B*'s new Share $= \frac{2}{6} - \frac{1}{16} = \frac{16-3}{48} = \frac{13}{48}$

C's new Share $= \frac{1}{6} - \frac{1}{16} = \frac{8-3}{48} = \frac{5}{48}$ *D*'s Share $= \frac{1}{8}$

Thus, the New Profit Sharing Ratio for *A, B, C* and *D* will be : $\frac{3}{6} : \frac{13}{48} : \frac{5}{48} : \frac{1}{8}$

$$= \frac{24:13:5:6}{48} = 24:13:5:6$$

(3) Sometimes the new partner 'purchases' his share from the old partners in a particular ratio. In such cases the new profit sharing ratio of the old partners will be calculated after deducting the sacrifice made by a partner from his existing share of profit.

ILLUSTRATION 3.

(*a*) *A* and *B* are partners sharing profits in the ratio of 7 : 3. *C* was admitted with $\frac{3}{7}$th share in the profits which he took $\frac{2}{7}$th from *A* and $\frac{1}{7}$th from *B*. Calculate new ratio of partners.

(*b*) Ram and Shyam are partners in a firm sharing profits in the ratio of 7 : 5. Mohan is admitted on $\frac{1}{6}$th share which he takes $\frac{1}{24}$th from Ram and $\frac{1}{8}$th from Shyam. Calculate the new profit sharing ratio of the partners.

SOLUTION :

(*a*) *A*'s share $= \frac{7}{10} - \frac{2}{7} = \frac{49-20}{70} = \frac{29}{70}$

B's share $= \frac{3}{10} - \frac{1}{7} = \frac{21-10}{70} = \frac{11}{70}$

C's share $= \frac{2}{7} + \frac{1}{7} = \frac{3}{7}$

Thus the new profit sharing ratio for *A, B* and *C* will be :

$$\frac{29}{70} : \frac{11}{70} : \frac{3}{7} \text{ or } \frac{29:11:30}{70} \text{ or } 29:11:30$$

(*b*) Ram's old share is $\frac{7}{12}$, out of which he surrenders $\frac{1}{24}$th in favour of Mohan.

Therefore, Ram's new share is $= \frac{7}{12} - \frac{1}{24} = \frac{14-1}{24} = \frac{13}{24}$

Shyam's old share is $\frac{5}{12}$, out of which he surrenders $\frac{1}{8}$th in favour of Mohan.

Therefore, Shyam's new share is $= \frac{5}{12} - \frac{1}{8} = \frac{10-3}{24} = \frac{7}{24}$

Mohan's share $= \frac{1}{6}$ or $\frac{4}{24}$

Therefore, New ratio of Ram, Shyam and Mohan will be 13 : 7 : 4.

ILLUSTRATION 4.

(*a*) Lucy and Zeny were partners in a firm sharing profits in 4 : 3 ratio. They admitted Allen as a new partner for 20% of share in the profits. Allen acquired his share of profits in the ratio of 1 : 2 from Lucy and Zeny. Calculate the new profit sharing ratio of Lucy, Zeny and Allen.

(*b*) *A*, *B* and *C* are partners sharing profits in 3 : 2 : 2 ratio. They admitted *D* as a new partner for 1/5 share which he acquired from *A*, *B* and *C* in 2 : 2 : 1 ratio respectively. Calculate new profit sharing ratio.

SOLUTION :

(*a*) Allen acquired her share of profit (20% or $\frac{1}{5}$) from Lucy and Zeny in the ratio of 1 : 2. This means

Allen gets $\frac{1}{3}$ of $\frac{1}{5}$ $= \frac{1}{15}$ from Lucy

Allen gets $\frac{2}{3}$ of $\frac{1}{5}$ $= \frac{2}{15}$ from Zeny

Hence, the new ratio of Lucy $= \frac{4}{7} - \frac{1}{15} = \frac{60-7}{105} = \frac{53}{105}$

new ratio of Zeny $= \frac{3}{7} - \frac{2}{15} = \frac{45-14}{105} = \frac{31}{105}$

Thus, the new profit sharing ratio of Lucy, Zeny and Allen will be :

$$\frac{53}{105} : \frac{31}{105} : \frac{1}{5} \text{ or } \frac{53:31:21}{105} = 53:31:21$$

(*b*) *D*'s share is $\frac{1}{5}$ which he acquired from *A*, *B* and *C* in 2 : 2 : 1. This means

D gets $\frac{2}{5}$ of $\frac{1}{5}$ $= \frac{2}{25}$ from *A*

D gets $\frac{2}{5}$ of $\frac{1}{5}$ $= \frac{2}{25}$ from *B*

D gets $\frac{1}{5}$ of $\frac{1}{5}$ $= \frac{1}{25}$ from *C*

Hence, the new ratio of $A = \frac{3}{7} - \frac{2}{25} = \frac{75-14}{175} = \frac{61}{175}$

the new ratio of $B = \frac{2}{7} - \frac{2}{25} = \frac{50-14}{175} = \frac{36}{175}$

the new ratio of $C = \frac{2}{7} - \frac{1}{25} = \frac{50-7}{175} = \frac{43}{175}$

D's share $= \frac{1}{5}$

Thus, the new profit sharing ratio of *A, B, C* and *D* will be :

$$\frac{61}{175} : \frac{36}{175} : \frac{43}{175} : \frac{1}{5} \text{ or } \frac{61:36:43:35}{175} \text{ or } 61:36:43:35$$

ILLUSTRATION 5.

A and *B* are partners in a firm sharing profits and losses in the ratio of 3 : 2. *C* is admitted for 1/5th share in profits of the firm. Calculate the new profit sharing ratio of the partners if,

(*a*) *C* gets it equally from *A* and *B*
(*b*) *C* gets it from *A* and *B* in the ratio of 2 : 1
(*c*) *C* gets it wholly from *A*
(*d*) *C* gets it wholly from *B*
(*e*) *C* gets it 3/20 from *A* and 1/20 from *B*.

SOLUTION :

(*a*) If *C* gets his share equally from *A* and *B* :

Share acquired by C from $A = \frac{1}{2}$ of $\frac{1}{5} = \frac{1}{10}$

Share acquired by C from $B = \frac{1}{2}$ of $\frac{1}{5} = \frac{1}{10}$

Hence, A's new share $= \frac{3}{5} - \frac{1}{10} = \frac{6-1}{10} = \frac{5}{10}$

B's new share $= \frac{2}{5} - \frac{1}{10} = \frac{4-1}{10} = \frac{3}{10}$

C's share $= \frac{1}{5}$

New Ratios $= \frac{5}{10} : \frac{3}{10} : \frac{1}{5} = \frac{5:3:2}{10} = 5:3:2$

(*b*) If *C* gets his share from *A* and *B* in the ratio of 2 : 1

Share acquired by C from $A = \frac{2}{3}$ of $\frac{1}{5} = \frac{2}{15}$

Share acquired by C from $B = \frac{1}{3}$ of $\frac{1}{5} = \frac{1}{15}$

Hence, A's new share $= \frac{3}{5} - \frac{2}{15} = \frac{9-2}{15} = \frac{7}{15}$

B's new share $= \frac{2}{5} - \frac{1}{15} = \frac{6-1}{15} = \frac{5}{15}$

C's share $= \frac{1}{5}$

New Ratios $= \frac{7}{15} : \frac{5}{15} : \frac{1}{5} = \frac{7:5:3}{15} = 7:5:3$

(*c*) If *C* gets his share wholly from *A*

Hence, *A*'s new share $= \frac{3}{5} - \frac{1}{5} = \frac{2}{5}$

B's share $= \frac{2}{5}$

C's share $= \frac{1}{5}$

New Ratios = 2 : 2 : 1

(*d*) If *C* gets his share wholly from *B* :

A's share $= \frac{3}{5}$

B's new share $= \frac{2}{5} - \frac{1}{5} = \frac{1}{5}$

C's share $= \frac{1}{5}$

New Ratios = 3 : 1 : 1

(*e*) If *C* gets 3/20 from *A* and 1/20 from *B*

A's new share $= \frac{3}{5} - \frac{3}{20} = \frac{12-3}{20} = \frac{9}{20}$

B's new share $= \frac{2}{5} - \frac{1}{20} = \frac{8-1}{20} = \frac{7}{20}$

C's share $= \frac{3}{20} + \frac{1}{20} = \frac{4}{20}$

New Ratios = 9 : 7 : 4.

ILLUSTRATION 6.

Arun, Bhushan and Chetan are partners in a firm sharing profits in 3 : 2 : 3 ratio. They decide to admit Sehzad as a partner. Arun surrendered 1/3 of his share in favour of Sehzad, Bhushan surrendered 1/4 of his share in favour of Sehzad and Chetan surrendered 1/5 of his share in favour of Sehzad. Calculate new profit sharing ratio.

SOLUTION :

(*i*) Calculation of Surrendered share :

Arun's old share $= \frac{3}{8}$, Arun surrenders $\frac{1}{3}$ of $\frac{3}{8}$ in favour of Sehzad, *i.e.*, $\frac{1}{3} \times \frac{3}{8} = \frac{1}{8}$

Bhushan's old share $= \frac{2}{8}$, Bhushan surrenders $\frac{1}{4}$ of $\frac{2}{8}$ in favour of Sehzad, *i.e.*,

$\frac{1}{4} \times \frac{2}{8} = \frac{1}{16}$

Chetan's old share $= \frac{3}{8}$, Chetan surrenders $\frac{1}{5}$ of $\frac{3}{8}$ in favour of Sehzad, *i.e.*,

$$\frac{1}{5} \times \frac{3}{8} = \frac{3}{40}$$

Calculation of New Ratios :

Arun's new share after surrendering $\frac{1}{8}$ in favour of Sehzad

$$= \frac{3}{8} - \frac{1}{8} = \frac{2}{8}$$

Bhushan's new share after surrendering $\frac{1}{16}$ in favour of Sehzad

$$= \frac{2}{8} - \frac{1}{16} = \frac{4-1}{16} = \frac{3}{16}$$

Chetan's new share after surrendering $\frac{3}{40}$ in favour of Sehzad

$$= \frac{3}{8} - \frac{3}{40} = \frac{15-3}{40} = \frac{12}{40}$$

Sehzad's share is the total of $\frac{1}{8}$ from Arun, $\frac{1}{16}$ from Bhushan and $\frac{3}{40}$ from Chetan

$$= \frac{1}{8} + \frac{1}{16} + \frac{3}{40} = \frac{10+5+6}{80} = \frac{21}{80}$$

Hence, New Ratio of Arun, Bhushan, Chetan and Sehzad

$$= \frac{2}{8} : \frac{3}{16} : \frac{12}{40} : \frac{21}{80} = \frac{20:15:24:21}{80} = 20:15:24:21$$

ILLUSTRATION 7.

Ram and Mohan were partners in a firm sharing profits in 3 : 2 ratio. On 1st April 2020, they admitted Sita and Radha as new partners. Ram sacrificed 1/3rd of his share in favour of Sita and Mohan sacrificed 1/2 of his share in favour of Radha. Profit of the firm for the year ended 31st March 2021 amounted to ₹3,60,000. Prepare necessary journal entries for distribution of profit.

SOLUTION:

JOURNAL

Date	*Particulars*	*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2021				
March 31	Profit & Loss A/c Dr.		3,60,000	
	To Profit & Loss Appropriation A/c			3,60,000
	(Transfer of profit to Profit & Loss Appropriation A/c)			
March 31	Profit & Loss Appropriation A/c Dr.		3,60,000	
	To Ram's Capital A/c			1,44,000
	To Mohan's Capital A/c			72,000
	To Sita's Capital A/c			72,000
	To Radha's Capital A/c			72,000
	(Distribution of profit in the ratio of 2 : 1 : 1 : 1)			

Working Notes :

Calculation of Surrendered Share :

(*i*) Ram's old share $= \frac{3}{5}$; Ram surrenders $\frac{1}{3}$rd of $\frac{3}{5}$ in favour of Sita, *i.e.*,

$\frac{1}{3} \times \frac{3}{5} = \frac{1}{5}$ (It means Ram has surrendered $\frac{1}{5}$ out of his share in favour of Sita.)

(*ii*) Mohan's old share $= \frac{2}{5}$; Mohan surrenders $\frac{1}{2}$ of $\frac{2}{5}$ in favour of Radha, *i.e.*,

$\frac{1}{2}$ of $\frac{2}{5} = \frac{1}{5}$ (It means Mohan has surrendered $\frac{1}{5}$ out of his share in favour of Radha.)

Calculation of New Ratios :

Ram $= \frac{3}{5} - \frac{1}{5} = \frac{2}{5}$

Mohan $= \frac{2}{5} - \frac{1}{5} = \frac{1}{5}$

Sita $= \frac{1}{5}$

Radha $= \frac{1}{5}$

New Ratio = 2 : 1 : 1 : 1

ILLUSTRATION 8.

On 1-4-2019 Sahil and Charu entered into partnership for sharing profits in the ratio of 4 : 3. They admitted Tanu as a new partner on 1-4-2021 for $\frac{1}{5}$th share which she acquired equally from Sahil and Charu. To meet the requirements of additional capital they admitted Puneet as a new partner on 1-4-2022 for $\frac{1}{7}$th share in profits which he acquired from Sahil and Charu in 7 : 3 ratio.

Calculate :

(*i*) New profit sharing ratio of Sahil, Charu and Tanu for the year 2021-22.

(*ii*) New profit sharing ratio of Sahil, Charu, Tanu and Puneet on Puneet's admission.

SOLUTION :

(1) Calculation of New Profit Sharing Ratio of Sahil, Charu and Tanu :

Share of Profit given to Tanu $= \frac{1}{5}$

Share acquired by Tanu from Sahil $= \frac{1}{2}$ of $\frac{1}{5} = \frac{1}{10}$

Share acquired by Tanu from Charu $= \frac{1}{2}$ of $\frac{1}{5} = \frac{1}{10}$

Hence, Sahil's new share $= \frac{4}{7} - \frac{1}{10} = \frac{40-7}{70} = \frac{33}{70}$

Charu's new share $= \frac{3}{7} - \frac{1}{10} = \frac{30-7}{70} = \frac{23}{70}$

Tanu's new share $= \frac{1}{10} + \frac{1}{10} = \frac{2}{10}$

Thus, New Profit Sharing Ratio among Sahil, Charu and Tanu will be

$$\frac{33}{70} : \frac{23}{70} : \frac{2}{10} \text{ or } \frac{33 : 23 : 14}{70} \text{ or } 33 : 23 : 14$$

(2) Calculation of New Profit Sharing Ratio of Sahil, Charu, Tanu and Puneet :

Share of Profit given to Puneet $= \frac{1}{7}$

Share acquired by Puneet from Sahil $= \frac{7}{10} \text{ of } \frac{1}{7} = \frac{7}{70}$

Share acquired by Puneet from Charu $= \frac{3}{10} \text{ of } \frac{1}{7} = \frac{3}{70}$

Hence, Sahil's new share $= \frac{33}{70} - \frac{7}{70} = \frac{26}{70}$

Charu's new share $= \frac{23}{70} - \frac{3}{70} = \frac{20}{70}$

Tanu's share $= \frac{14}{70}$

Puneet's share $= \frac{1}{7}$

Thus, New Profit Sharing Ratio among Sahil, Charu, Tanu and Puneet :

$$\frac{26}{70} : \frac{20}{70} : \frac{14}{70} : \frac{1}{7} \text{ or } \frac{26 : 20 : 14 : 10}{70} \text{ or } 26 : 20 : 14 : 10 = 13 : 10 : 7 : 5$$

ILLUSTRATION 9.

A and *B* are equal partners. They admit *C* and *D* as partners with 1/5 and 1/6 share respectively. What is the profit sharing ratio of all the partners?

SOLUTION.

Let total profit of the firm be 1

Shares of *C* and *D* is $\frac{1}{5}$ and $\frac{1}{6}$ respectively.

Balance remaining $= 1 - (\frac{1}{5} + \frac{1}{6}) = \frac{30 - (6 + 5)}{30} = \frac{19}{30}$

$\frac{19}{30}$ is to be shared equally by *A* and *B*

Hence, *A*'s share $= \frac{19}{30} \times \frac{1}{2} = \frac{19}{60}$

B's share $= \frac{19}{30} \times \frac{1}{2} = \frac{19}{60}$

New Profit sharing Ratio of *A*, *B*, *C* and *D* $= \frac{19}{60} : \frac{19}{60} : \frac{1}{5} : \frac{1}{6}$

$$\frac{19 : 19 : 12 : 10}{60}$$

or $19 : 19 : 12 : 10$

Sacrifice Ratio :

Whenever there is an admission of a new partner, old partners have to surrender some of their old shares in favour of the new partner. The ratio in which they surrender their profits is called sacrifice ratio. Goodwill is paid to the old partners in their sacrifice ratio because the goodwill is the amount of compensation to be paid by the new partner to the old partners for acquiring the share of profits which they have surrendered in favour of the new partner.

Calculation : Sacrifice Ratio is calculated as follows :

Sacrifice Ratio = Old Ratio – New Ratio

ILLUSTRATION 10.

A, B and *C* are partners sharing profits in the ratio of 5 : 3 : 2. They admit *D* into partnership. The new profit sharing ratio of partners is 3 : 2 : 2 : 3. Calculate the sacrificing ratio.

SOLUTION :

Sacrifice Ratio = Old Ratio – New Ratio

Therefore, Sacrifice made by $A = \frac{5}{10} - \frac{3}{10} = \frac{2}{10}$

Sacrifice made by $B = \frac{3}{10} - \frac{2}{10} = \frac{1}{10}$

Sacrifice made by $C = \frac{2}{10} - \frac{2}{10} = 0$

C has not sacrificed any share of profit,

therefore sacrifice ratio of *A* and *B* $= \frac{2}{10} : \frac{1}{10}$ or 2 : 1.

Note : Old partners are entitled to the amount of goodwill in their sacrificing ratio. If any partner has made no sacrifice, he will not be entitled to any amount of goodwill. In the above illustration *C* has made no sacrifice. Therefore, he will not get any share in the goodwill.

ILLUSTRATION 11.

X, Y and *Z* share profits in the ratio of 4 : 3 : 2. *P* was admitted in the firm as a partner with 1/10th share of profits. Calculate sacrificing ratios of the partners.

SOLUTION :

For Calculating the sacrifice ratio we require old as well as new profit sharing ratios. But in this illustration new profit sharing ratios have not been given. Therefore, we will have to calculate the new profit ratios first of all.

Calculation of New Profit Sharing Ratios

Let total profit be = 1, *P* takes $= \frac{1}{10}$ th share out of 1, Remaining part is $1 - \frac{1}{10}$

$= \frac{9}{10}$

Thus the old partners will now share $\frac{9}{10}$ th share, which will be divided in their old profit sharing ratio of 4 : 3 : 2.

Therefore, X's new share of profit will be $= \frac{4}{9}$ of $\frac{9}{10} = \frac{4}{10}$

Y's new share of profit will be $= \frac{3}{9}$ of $\frac{9}{10} = \frac{3}{10}$

Z's new share of profit will be $= \frac{2}{9}$ of $\frac{9}{10} = \frac{2}{10}$

P's share $= \frac{1}{10}$

Thus, the new profit sharing ratio will be $= X : Y : Z : P$

$= \frac{4}{10} : \frac{3}{10} : \frac{2}{10} : \frac{1}{10} = 4 : 3 : 2 : 1$

Calculation of Sacrificing Ratios :

Sacrificing Ratio = Old Ratio – New Ratio

Therefore, Sacrifice made by X $= \frac{4}{9} - \frac{4}{10} = \frac{40-36}{90} = \frac{4}{90}$

Sacrifice made by Y $= \frac{3}{9} - \frac{3}{10} = \frac{30-27}{90} = \frac{3}{90}$

Sacrifice made by Z $= \frac{2}{9} - \frac{2}{10} = \frac{20-18}{90} = \frac{2}{90}$

Therefore, Sacrifice ratio of X, Y and Z $= \frac{4}{90} : \frac{3}{90} : \frac{2}{90} = 4 : 3 : 2$

ILLUSTRATION 12.

A and B are partners sharing profits in the ratio of 4 : 1. A surrenders 1/4th of his share and B surrenders 1/2 of his share in favour of C, a new partner. What is the sacrificing ratio and the new ratio?

SOLUTION :

(I) A surrenders $\frac{1}{4}$th of $\frac{4}{5}$ in favour of C. It means A has surrendered $\frac{1}{4} \times \frac{4}{5} = \frac{1}{5}$ out of his share in favour of C.

(II) B surrenders $\frac{1}{2}$ of $\frac{1}{5}$ in favour of C. It means B has surrendered $\frac{1}{2} \times \frac{1}{5}$ $= \frac{1}{10}$ out of his share in favour of C.

$\therefore$ Sacrificing Ratio $= A\frac{1}{5} : B\frac{1}{10} = 2 : 1.$

New Ratios: A's new share $= \frac{4}{5} - \frac{1}{5} = \frac{3}{5}$, B's new share $= \frac{1}{5} - \frac{1}{10} = \frac{1}{10}$

C's new share $= \frac{1}{5} + \frac{1}{10} = \frac{3}{10}$

Therefore, the new ratio of A, B and $C = \frac{3}{5} : \frac{1}{10} : \frac{3}{10}$ or 6 : 1 : 3

ILLUSTRATION 13.

Anil and Sunil are partners sharing profits and losses in the ratio of 3 : 2. They admit Charan as a new partner from 1st April, 2022. Anil gives 1/3rd of his share while Sunil gives 1/10th from his share to Charan. Calculate the sacrificing ratios and the new ratios.

SOLUTION :

(1) **Calculation of Sacrificing Ratios :**

(*i*) Anil's old share $= \frac{3}{5}$; He surrenders $\frac{1}{3}$ of his share

Hence, share surrendered by Anil $= \frac{3}{5} \times \frac{1}{3} = \frac{1}{5}$

(*ii*) Sunil's old share $= \frac{2}{5}$; He surrenders $\frac{1}{10}$ from his share

Hence, share surrendered by Sunil $= \frac{1}{10}$

Sacrifice Ratio $= \frac{1}{5} : \frac{1}{10}$ or 2 : 1

(2) **Calculation of New Ratios :**

Anil $= \frac{3}{5} - \frac{1}{5} = \frac{2}{5}$

Sunil $= \frac{2}{5} - \frac{1}{10} = \frac{4-1}{10} = \frac{3}{10}$

Charan $= \frac{1}{5} + \frac{1}{10} = \frac{2+1}{10} = \frac{3}{10}$

Hence, New ratio of Anil, Sunil and Charan $= \frac{2}{5} : \frac{3}{10} : \frac{3}{10}$ or 4 : 3 : 3

ILLUSTRATION 14.

Find out the sacrificing ratio and new ratio in the following cases :

(*a*) *A* and *B* are partners sharing profits and losses in the ratio of 3 : 2. *C* is admitted for 1/4th share. *A* and *B* decide to share equally in future.

(*b*) *A* and *B* are partners. They admit '*C*' for $\frac{1}{4}$th share. In future the ratio between *A* and *B* would be 2 : 1.

SOLUTION :

(*a*) **Calculation of new profit sharing ratio :**

C's share $= \frac{1}{4}$, The remaining share $= \frac{3}{4}$, This is to be shared equally by *A* and *B*.

Hence, the new share of $A = \frac{1}{2}$ of $\frac{3}{4} = \frac{3}{8}$, New share of $B = \frac{1}{2}$ of $\frac{3}{4} = \frac{3}{8}$

Thus, New Profit sharing ratio $= \frac{3}{8} : \frac{3}{8} : \frac{1}{4}$ or 3 : 3 : 2

Calculation of sacrificing ratio : Sacrificing Ratio = Old Ratio – New Ratio

Sacrifice made by $A = \frac{3}{5} - \frac{3}{8} = \frac{24-15}{40} = \frac{9}{40}$

Sacrifice made by $B = \frac{2}{5} - \frac{3}{8} = \frac{16-15}{40} = \frac{1}{40}$

Thus, Sacrificing Ratio between A and B is 9 : 1.

(*b*) **Calculation of new profit sharing ratio :**

C's share $= \frac{1}{4}$; Remaining Share $= \frac{3}{4}$

This is to be shared by A and B in the ratio of 2 : 1.

Hence, the new share of $A = \frac{2}{3}$ of $\frac{3}{4} = \frac{1}{2}$

new share of $B = \frac{1}{3}$ of $\frac{3}{4} = \frac{1}{4}$

Thus, New Profit sharing ratio $= \frac{1}{2} : \frac{1}{4} : \frac{1}{4}$ or 2 : 1 : 1

Calculation of Sacrificing Ratio : Sacrificing Ratio = Old Ratio – New Ratio

Sacrifice made by $A = \frac{1}{2} - \frac{1}{2} = 0$

Sacrifice made by $B = \frac{1}{2} - \frac{1}{4} = \frac{1}{4}$

Thus, the whole sacrifice is made by B.

ILLUSTRATION 15.

X and Y are sharing profits and losses in the ratio of 5 : 3. Z is admitted and it is decided that the profit sharing ratio between Y and Z shall be the same as existing between X and Y. Calculate the new profit sharing ratio and the sacrificing ratio.

SOLUTION :

The ratio between X and Y is 5 : 3. Hence, the ratio between Y and Z should also be the same *i.e.*, 5 : 3 (or $Y\frac{5}{8}, Z\frac{3}{8}$).

Thus, If the ratio of Y is 5, the ratio of Z should be = 3

If the ratio of Y is $\frac{3}{8}$, the ratio of Z should be $= \frac{3}{5} \times \frac{3}{8} = \frac{9}{40}$

New Profit Sharing Ratio $= \frac{5}{8} : \frac{3}{8} : \frac{9}{40} = \frac{25 : 15 : 9}{40}$ or 25 : 15 : 9

Calculation of Sacrificing Ratio :

Sacrificing Ratio = Old Share – New Share

X's Sacrifice $= \frac{5}{8} - \frac{25}{49} = \frac{45}{392}$;

Y's Sacrifice $= \frac{3}{8} - \frac{15}{49} = \frac{27}{392}$

Sacrificing Ratio of X and $Y = \frac{45}{392} : \frac{27}{392} = 45 : 27$ or 5 : 3

ILLUSTRATION 16.

K, L and M partners sharing in the ratio of 3 : 2 : 1. They admit N for $\frac{1}{6}$th share. It is agreed that M would retain his original share. Calculate the new ratios and sacrificing ratios.

SOLUTION :

Calculation of New Profit Sharing Ratio :

N's share $= \frac{1}{6}$; $\quad$ M's share $= \frac{1}{6}$

Remaining share for K and $L = 1 - (\frac{1}{6} + \frac{1}{6}) = \frac{4}{6}$

This will be divided between K and L in their old ratio *i.e.,* 3 : 2

Hence, the new share of $K = \frac{3}{5}$ of $\frac{4}{6} = \frac{12}{30}$

new share of $L = \frac{2}{5}$ of $\frac{4}{6} = \frac{8}{30}$

Thus, the new ratio of K, L, M and $N = \frac{12}{30} : \frac{8}{30} : \frac{1}{6} : \frac{1}{6}$ or 12 : 8 : 5 : 5

Calculation of Sacrificing Ratio :

Sacrifice made by $K = \frac{3}{6} - \frac{12}{30} = \frac{3}{30}$

Sacrifice made by $L = \frac{2}{6} - \frac{8}{30} = \frac{2}{30}$

Sacrifice made by M = NIL

Thus, Sacrificing Ratio among K, L and M = 3 : 2 : 0

ILLUSTRATION 17.

A, B and C are partners sharing profits and losses in the ratio of 9 : 6 : 5. D is admitted as a new partner for 1/4th share. B sacrifices 1/20th from his share in favour of D and rest of the sacrifice was made by A and C in the ratio of 3 : 1. Calculate sacrificing ratio and new profit sharing ratio.

SOLUTION :

(*i*) **Calculation of Sacrificing Ratio :**

D's share $= \frac{1}{4}$, Out of which $\frac{1}{20}$ is given by B.

Remaining Share of $D = \frac{1}{4} - \frac{1}{20} = \frac{5-1}{20} = \frac{4}{20}$

This $\frac{4}{20}$ share is sacrificed by A and C in the ratio of 3 : 1

Hence, A's Sacrifice $= \frac{4}{20} \times \frac{3}{4} = \frac{3}{20}$

C's Sacrifice $= \frac{4}{20} \times \frac{1}{4} = \frac{1}{20}$

Sacrifice Ratio of A, B and $C = \frac{3}{20} : \frac{1}{20} : \frac{1}{20}$ or 3 : 1 : 1

(ii) Calculation of New Ratio :

$A : \frac{9}{20} - \frac{3}{20} = \frac{6}{20}$

$B : \frac{6}{20} - \frac{1}{20} = \frac{5}{20}$

$C : \frac{5}{20} - \frac{1}{20} = \frac{4}{20}$

$D : \frac{1}{4}$ or $\frac{5}{20}$

New Ratio of A, B, C and $D = \frac{6}{20} : \frac{5}{20} : \frac{4}{20} : \frac{5}{20}$ or 6 : 5 : 4 : 5.

CASE BASED MCQs — 1

Dev, Gautam and Kamal were three partners sharing profits and losses in the ratio of 2 : 1 : 2. On 1st April, 2020, their capital account balances stood at ₹90,000, ₹80,000 and ₹20,000 (Dr.) respectively.

On this date they admitted Naveen into the partnership with a capital of ₹50,000.

Naveen is to have 1/4 share of the profits with a guaranteed minimum share of distributable profit of ₹40,000.

The new profit-sharing ratio among the partners being Dev : Gautam : Kamal : Naveen = 6 : 2 : 7 : 5.

The profit of the firm for the year 2020-21 was ₹1,60,000 before the following adjustments were made :

- Interest on Capital @ 10% per annum to be allowed to the partners.
- Interest on Drawings : Dev : ₹3,000; Kamal : ₹6,000.
- Salary to Partners : Gautam ₹7,000; Naveen : ₹10,000.

(a) The sacrificing ratio of Dev, Gautam and Kamal will be :

(i) 1 : 2 : 2 (ii) 2 : 2 : 1
(iii) 1 : 1 : 2 (iv) 2 : 1 : 2

(b) The total interest on capital allowed by the firm to the partners will be :

(i) ₹22,000 (ii) ₹23,000
(iii) ₹21,400 (iv) ₹23,100

(c) Deficiency in Naveen's profits will be :

(i) ₹ 8,000 (ii) ₹ 7,500
(iii) ₹12,500 (iv) ₹12,000

(ISC Sample Paper, 2021)

(See Answers at the end of the book)

Accounting Treatment of Goodwill on the Admission of a New Partner :

There may be three situations related to treatment of goodwill (premium) at the time of admission of a new partner :

(1) When the amount of goodwill (premium) is paid privately;

(2) When the new partner brings his share of goodwill (premium) in Cash;

(3) When the new partner does not bring his share of goodwill (premium) in Cash.

These situations are discussed below :

(1) **When the Amount of Goodwill (premium) is Paid Privately :—** When the new partner pays the amount of goodwill in cash to the old partners privately outside the business, no entries are required to be passed.

(2) **When the New Partner brings his Share of Goodwill (premium) in Cash :—** According to this method there are two alternatives :

(*i*) **When the Amount of Goodwill/Premium brought in by the New Partner is Retained in the Business :—** If the new partner brings in his share of goodwill in cash and this amount is retained in the business, the amount is credited to the Capital Accounts of old partners in their sacrificing ratio. The following two entries are passed for this purpose :

(*a*) Cash/Bank A/c Dr.
To Premium for Goodwill A/c
(Amount of goodwill/premium brought in cash by new partner)

(*b*) Premium for Goodwill A/c Dr.
To Old Partners' Capital A/cs
(Amount of goodwill/premium transferred to old partners' capital accounts in sacrificing ratio)

(*ii*) **When Goodwill/Premium brought in by the New Partner is Withdrawn by the Old Partners :—** Sometimes, the amount of goodwill brought in by new partner is withdrawn by the old partners. In this case, in addition to the two Journal entries explained above in (*i*), one more Journal entry is required to be passed :

Old Partner's Capital A/cs Dr.
To Cash/Bank A/c
(Amount of goodwill/premium withdrawn by the old partners)

It must be noted that sometimes partners withdraw only ½ or ¼th amount of goodwill. In such cases, entry should be passed with the withdrawn amount only.

ILLUSTRATION 18.

A and *B* are partners in a firm, sharing Profits and Losses in the ratio of 3 : 2. Their capitals are ₹1,80,000 and ₹1,40,000 respectively. They admit *X* in partnership on the conditions that he will bring ₹67,500 as goodwill and ₹1,50,000 as capital and will get 1/4 share in the profits of the firm. Assuming that the capital and goodwill have been brought in cash by the new partner, pass the necessary journal entries and find out new profit sharing ratio of partners when (A) Goodwill is retained in the firm and (B) Goodwill is withdrawn by old partners.

SOLUTION:

(A) When the amount of Goodwill is not withdrawn by the old partners:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.		2,17,500	
	To *X*'s Capital A/c				1,50,000
	To Premium for Goodwill A/c				67,500
	(Amount of capital and goodwill/premium brought in cash by new partner)				
	Premium for Goodwill A/c(1)	Dr.		67,500	
	To *A*'s Capital A/c				40,500
	To *B*'s Capital A/c				27,000
	(Amount of goodwill/premium credited to the old partner's capitals in Sacrifice Ratio *i.e.*, 3 : 2)				

(B) When the amount of Goodwill is withdrawn by the old partners :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.		2,17,500	
	To *X*'s Capital A/c				1,50,000
	To Premium for Goodwill A/c				67,500
	(Amount of capital and goodwill/premium brought in cash by new partner)				
	Premium for Goodwill A/c(1)	Dr.		67,500	
	To *A*'s Capital A/c				40,500
	To *B*'s Capital A/c				27,000
	(Amount of goodwill/premium credited to old partner's capitals in sacrifice ratio *i.e.*, 3 : 2)				
	A's Capital A/c	Dr.		40,500	
	B's Capital A/c	Dr.		27,000	
	To Bank A/c				67,500
	(Amount of goodwill/premium withdrawn by the old partners)				

Calculation of New Profit Sharing Ratios :

Let total profit be $= 1$

X is given $\frac{1}{4}$ th share out of 1; Remaining profit is $= 1 - \frac{1}{4} = \frac{3}{4}$

Old partners will now share only $\frac{3}{4}$ th profit, in their old profit sharing ratio :

Therefore, A's new share of profit $= \frac{3}{5}$ of $\frac{3}{4} = \frac{9}{20}$

B's new share of profit $= \frac{2}{5}$ of $\frac{3}{4} = \frac{6}{20}$

X's share $= \frac{1}{4}$

Thus, the new profit sharing ratio of A, B and X will be :

$$A : B : X$$

$$= \frac{9}{20} : \frac{6}{20} : \frac{1}{4}$$

$$= \frac{9 : 6 : 5}{20} = 9 : 6 : 5.$$

Note : (1) As the new profit sharing ratio is not given in the question, therefore it will be presumed that the old profit sharing ratio will be the sacrificing ratio. *i.e.*, it will be presumed that the partners have sacrificed in their old ratio.

ILLUSTRATION 19.

X and Y are partners sharing profit and losses in the ratio of 2 : 1. They admit Z into partnership with 1/4th share in profits which he acquires equally from X and Y. Z brings in ₹1,65,000 as capital and ₹30,000 as goodwill in cash.

Pass entries and calculate new profit sharing ratios.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c	Dr.		1,95,000	
	To Z's Capital A/c				1,65,000
	To Premium for Goodwill A/c				30,000
	(Amount of capital and goodwill/premium brought in cash)				
	Premium for Goodwill A/c	Dr.		30,000	
	To X's Capital A/c				15,000
	To Y's Capital A/c				15,000
	(Goodwill/premium transferred to old partners capitals in sacrifice ratio *i.e.*, equally)				

Calculation of new profit sharing ratios :

Z's share is $\frac{1}{4}$ which he acquires equally from X and Y.

Therefore, Z gets his share from X $= \frac{1}{2}$ of $\frac{1}{4} = \frac{1}{8}$

Z gets his share from Y $= \frac{1}{2}$ of $\frac{1}{4} = \frac{1}{8}$

New Ratio of X $= \frac{2}{3} - \frac{1}{8} = \frac{13}{24}$

New Ratio of Y $= \frac{1}{3} - \frac{1}{8} = \frac{5}{24}$

Thus, $X : Y : Z$

$$\frac{13}{24} : \frac{5}{24} : \frac{1}{4} = \frac{13 : 5 : 6}{24} = 13 : 5 : 6 \text{ New Ratio.}$$

ILLUSTRATION 20.

Ram and Shyam are partners. Their profit sharing ratio is 3 : 2. Mohan joins the partnership for 1/4th share in profits (of which he acquires 2/3 from Ram and 1/3 from Shyam). Mohan brings in ₹6,00,000 for capital and ₹2,40,000 for goodwill. 1/4 of the amount of goodwill is withdrawn by old partners.

Pass necessary Journal entries and find out new profit sharing ratio.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c	Dr.		8,40,000	
	To Mohan's Capital A/c				6,00,000
	To Premium for Goodwill A/c				2,40,000
	(Amount of capital and goodwill/premium brought in cash)				
	Premium for Goodwill A/c	Dr.		2,40,000	
	To Ram's Capital A/c				1,60,000
	To Shyam's Capital A/c				80,000
	(Goodwill/premium credited to old partners in their sacrifice ratio, *i.e.*, 2 : 1)				
	Ram's Capital A/c	Dr.		40,000	
	Shyam's Capital A/c	Dr.		20,000	
	To Bank A/c				60,000
	(One-fourth of the goodwill/premium withdrawn by old partners in cash)				

Calculation of new profit sharing ratios :

Mohan takes his share from Ram $= \frac{2}{3} \text{ of } \frac{1}{4} = \frac{2}{12} \text{ or } \frac{1}{6}$

Mohan takes his share from Shyam $= \frac{1}{3} \text{ of } \frac{1}{4} = \frac{1}{12}$

Therefore, Ram's new share $= \frac{3}{5} - \frac{1}{6} = \frac{13}{30}$

Shyam's new share $= \frac{2}{5} - \frac{1}{12} = \frac{19}{60}$

Mohan's share $= \frac{1}{4}$

Therefore, New profit sharing ratio of Ram, Shyam and Mohan

$$= \frac{13}{30} : \frac{19}{60} : \frac{1}{4} = \frac{26 : 19 : 15}{60}$$

$$= 26 : 19 : 15.$$

ILLUSTRATION 21.

A and *B* are partners sharing profits in the ratio of 3 : 2. They admit *C* into the firm for 3/7th profit which he takes 2/7th from *A* and 1/7th from *B*. *C* brings ₹60,000 for his share of goodwill and ₹2,00,000 for his capital.

Give necessary Journal entries. Also calculate new profit sharing ratio.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c	Dr.		2,60,000	
	To *C*'s Capital A/c				2,00,000
	To Premium for Goodwill A/c				60,000
	(Amount of capital and goodwill/premium brought in cash)				
	Premium for Goodwill A/c	Dr.		60,000	
	To *A*'s Capital A/c				40,000
	To *B*'s Capital A/c				20,000
	(Goodwill/premium transferred to old partners capitals in sacrifice ratio, *i.e.*, 2 : 1)				

New Ratios : $A = \frac{3}{5} - \frac{2}{7} = \frac{11}{35}$

$B = \frac{2}{5} - \frac{1}{7} = \frac{9}{35}$

$C = \frac{3}{7}$ or $\frac{15}{35}$ $\qquad A : B : C \qquad 11 : 9 : 15$

ILLUSTRATION 22.

A and *B* share profits and losses in the ratio of 5 : 3. They admit *C* as a partner who pays ₹54,000 as premium for goodwill for $\frac{1}{5}$th share in the future profits of the firm. Pass Journal Entries appropriating the premium money and show the new profit sharing ratio in each of the following cases :

(*i*) if he acquires his share of profits in the original ratio of existing partners;

(*ii*) if he acquires his share of profits in equal proportions from the existing partners;

(*iii*) if he acquires his share in the ratio of 3 : 1 from the existing partners;

(*iv*) if he acquires his share of profits as 1/6th from *A* and 1/30th from *B*.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c	Dr.		54,000	
	To Premium for Goodwill A/c				54,000
	(Premium for goodwill brought in Cash)				

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
First Case :	Premium for Goodwill A/c	Dr.		54,000	
	To *A*'s Capital A/c				33,750
	To *B*'s Capital A/c				20,250
	(Premium brought in by *C* credited to *A* and *B* in the sacrificing ratio of 5 : 3)				

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
Second Case:	Premium for Goodwill A/c	Dr.		54,000	
	To *A*'s Capital A/c				27,000
	To *B*'s Capital A/c				27,000
	(Premium brought in by *C* credited to *A* and *B* in the sacrificing ratio of 1 : 1)(1)				

Note 1. *C* acquires $\frac{1}{2}$ of $\frac{1}{5}$ or $\frac{1}{10}$ from each of *A* and *B*.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
Third Case :	Premium for Goodwill A/c	Dr.		54,000	
	To *A*'s Capital A/c				40,500
	To *B*'s Capital A/c				13,500
	(Premium brought in by *C* credited to *A* and *B* in the sacrificing ratio of 3 : 1)				

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
Fourth Case:	Premium for Goodwill A/c	Dr.		54,000	
	To *A*'s Capital A/c				45,000
	To *B*'s Capital A/c				9,000
	(Premium brought in by *C* credited to *A* and *B* in the sacrificing ratio of 5 : 1)(2)				

Note 2. Sacrificing ratio is $\frac{1}{6} : \frac{1}{30}$ or $\frac{5}{30} : \frac{1}{30}$ or 5 : 1.

Calculation of new profit sharing ratio :

First Case :

$A : \frac{5}{8} \text{ of } \frac{4}{5} = \frac{1}{2} \text{ or } \frac{5}{10}$ $\quad B : \frac{3}{8} \text{ of } \frac{4}{5} = \frac{3}{10}$ $\quad C : \frac{1}{5} = \frac{2}{10}$

Second Case :

$A : \frac{5}{8} - \frac{1}{10} = \frac{21}{40}$ $\quad B : \frac{3}{8} - \frac{1}{10} = \frac{11}{40}$ $\quad C : \frac{1}{5} = \frac{8}{40}$

Third Case :

C takes his share from $A = \frac{3}{4} \text{ of } \frac{1}{5} = \frac{3}{20}$ $\quad$ *C* takes his share from $B = \frac{1}{4} \text{ of } \frac{1}{5} = \frac{1}{20}$

$\therefore$ *A*'s share $= \frac{5}{8} - \frac{3}{20} = \frac{25-6}{40} = \frac{19}{40}$ $\quad$ *B*'s share $= \frac{3}{8} - \frac{1}{20} = \frac{15-2}{40} = \frac{13}{40}$

C's share $= \frac{1}{5} = \frac{8}{40}$

Fourth Case :

$A : \frac{5}{8} - \frac{1}{6} = \frac{11}{24}$ or $\frac{55}{120}$ $B : \frac{3}{8} - \frac{1}{30} = \frac{41}{120}$ $C : \frac{1}{6} + \frac{1}{30} = \frac{6}{30}$ or $\frac{24}{120}$

ILLUSTRATION 23.

A, *B* and *C* are partners, sharing profits in the ratio of 4 : 3 : 2. *D* is admitted for 2/9 share of profits and brings ₹3,00,000 as his capital and his share of goodwill in cash. The new profit sharing ratio will be *A* : *B* : *C* : *D*. 3 : 2 : 2 : 2.

Goodwill of the firm is valued at 150% of the average profits of last three years, which were as follows :

	₹
Year ended 31st March, 2018 (after charging loss by fire ₹60,000)	45,000
Year ended 31st March, 2019	2,40,000
Year ended 31st March, 2020	3,00,000

On 1st January 2020, a motorbike costing ₹80,000 was purchased and was wrongly debited to travelling expenses. Depreciation on motorbike was to be charged @ 25% p.a.

Journalise the above arrangement in the books.

SOLUTION

Books of *A*, *B*, *C* and *D*

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Bank A/c	Dr.		3,80,000	
	To *D*'s Capital A/c				3,00,000
	To Premium for Goodwill A/c				80,000
	(Amount of capital and goodwill/premium brought in cash)				
	Premium for Goodwill A/c	Dr.		80,000	
	To *A*'s Capital A/c				40,000
	To *B*'s Capital A/c				40,000
	(Amount of goodwill/premium transferred to old partners in sacrificing ratio, *i.e.*, 1 : 1)				

Working Notes :

(*i*) **Calculation of Goodwill :**

	₹	₹
Profit for the year ended 31st March, 2018 :	45,000	
Add : Abnormal Loss	60,000	1,05,000
Profit for the year ended 31st March, 2019 :		2,40,000
Profit for the year ended 31st March, 2020 :	3,00,000	
Add : Cost of Motorbike wrongly debited to P & L A/c	80,000	
	3,80,000	

Less :	Depreciation on Motorbike for 3 months : $80{,}000 \times \frac{25}{100} \times \frac{3}{12}$	5,000	3,75,000
			7,20,000

Average Profit : $7{,}20{,}000 \div 3 = ₹2{,}40{,}000$

Firm's Goodwill : $2{,}40{,}000 \times \frac{150}{100} = ₹3{,}60{,}000$

D's Share : $3{,}60{,}000 \times \frac{2}{9} = ₹\ 80{,}000$

(*ii*) **Calculation of Sacrificing Ratio :**

Sacrificing Ratio = Old Ratio – New Ratio

Thus, *A*'s Sacrifice Ratio $= \frac{4}{9} - \frac{3}{9} = \frac{1}{9}$

B's Sacrifice Ratio $= \frac{3}{9} - \frac{2}{9} = \frac{1}{9}$

C's Sacrifice Ratio $= \frac{2}{9} - \frac{2}{9} = 0$

As *C* has not made any sacrifice, therefore he will not be entitled to any amount of goodwill brought in by the new partner.

A and *B* have sacrificed in equal proportion, therefore they will get equal share in the goodwill brought in by *D*.

ILLUSTRATION 24.

A and *B* are in partnership sharing profits and losses in the ratio of 4 : 3. They admit *C* into the firm, *C* paying a premium of ₹14,000 for $\frac{1}{5}$ share of the profits. As between themselves, *A* and *B* agree to share future profits and losses equally. Draft journal entries.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c	Dr.		14,000	
	To Premium for Goodwill A/c				14,000
	(Amount of goodwill/premium brought in cash)				
	Premium for Goodwill A/c	Dr.		14,000	
	To *A*'s Capital A/c				12,000
	To *B*'s Capital A/c				2,000
	(Goodwill/premium transferred to old partners in sacrificing ratio of 6 : 1)				

Calculation of new profit sharing ratio : *C* takes $\frac{1}{5}$th share out of 1.

Thus, the remaining profit is $\frac{4}{5}$; This is divided equally between *A* and *B*.

A's new share $= \frac{4}{5} \times \frac{1}{2} = \frac{2}{5}$

B's new share $= \frac{4}{5} \times \frac{1}{2} = \frac{2}{5}$

Sacrifice made by $A = \frac{4}{7} - \frac{2}{5} = \frac{6}{35}$

Sacrifice made by $B = \frac{3}{7} - \frac{2}{5} = \frac{1}{35}$

Thus, the Sacrificing Ratio between A and B is 6 : 1.

ILLUSTRATION 25.

Kiya and Leela are partners sharing profits in the ratio of 3 : 2. Kiran was admitted as a new partner with 1/5th share in the profits and she brought in ₹24,000 as her share of goodwill premium that was credited to the capital accounts of Kiya and Leela respectively with ₹18,000 and ₹6,000.

Calculate the new profit sharing ratio of Kiya, Leela and Kiran.

(C.B.S.E. 2019, Rajasthan)

SOLUTION:

Sacrificing Ratio of Kiya and Leela = 18,000 : 6,000 = 3 : 1

Kiran's Share $= \frac{1}{5}$

Kiya's Sacrifice $= \frac{1}{5} \times \frac{3}{4} = \frac{3}{20}$

Leela's Sacrifice $= \frac{1}{5} \times \frac{1}{4} = \frac{1}{20}$

New Ratio = Old Ratio – Sacrificing Ratio

Kiya's New Share $= \frac{3}{5} - \frac{3}{20} = \frac{9}{20}$

Leela's New Share $= \frac{2}{5} - \frac{1}{20} = \frac{7}{20}$

Kiran's Share $= \frac{1}{5}$

New Ratio $= \frac{9}{20} : \frac{7}{20} : \frac{1}{5}$ or 9 : 7 : 4

ILLUSTRATION 26.

A and B are partners sharing profits in the ratio of 3 : 1. On 1st April 2018, they admit C into partnership for $\frac{1}{5}$th share who pays ₹50,000 as premium privately. On 1st April 2019, they admit D into partnership for $\frac{1}{6}$th share who brings ₹40,000 as premium 75% of which is withdrawn by the existing partners. On 1st April 2020, E is admitted as a partner for $\frac{1}{7}$th share who brings ₹60,000 as premium which is retained in the business.

Pass journal entries for the above.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019 April 1	Bank A/c	Dr.		40,000	
	To Premium for Goodwill A/c				40,000
	(Premium for goodwill brought in by *D*)				
April 1	Premium for Goodwill A/c	Dr.		40,000	
	To *A*'s Capital A/c				24,000
	To *B*'s Capital A/c				8,000
	To *C*'s Capital A/c				8,000
	(Premium credited to *A*, *B* and *C* in the sacrificing ratio of 3 : 1 : 1)				
April 1	*A*'s Capital A/c	Dr.		18,000	
	B's Capital A/c	Dr.		6,000	
	C's Capital A/c	Dr.		6,000	
	To Bank A/c				30,000
	(75% of premium withdrawn by the old partners)				
2020 April 1	Bank A/c	Dr.		60,000	
	To Premium for Goodwill A/c				60,000
	(Premium for goodwill brought in by *E*)				
April 1	Premium for Goodwill A/c	Dr.		60,000	
	To *A*'s Capital A/c				30,000
	To *B*'s Capital A/c				10,000
	To *C*'s Capital A/c				10,000
	To *D*'s Capital A/c				10,000
	(Premium credited to *A*, *B*, *C* and *D* in the sacrificing ratio of 3 : 1 : 1 : 1)				

Working Notes :

(1) *C* has paid the premium privately and hence no entry is required to be passed for such payment.

(2) Calculation of profit sharing ratios :

(*i*) After *C*'s admission :

C is given $\frac{1}{5}$th share. Hence the remaining share is $1 - \frac{1}{5} = \frac{4}{5}$

A's share $= \frac{3}{4}$ of $\frac{4}{5} = \frac{3}{5}$

B's share $= \frac{1}{4}$ of $\frac{4}{5} = \frac{1}{5}$

C's share $= \frac{1}{5}$

(*ii*) After *D*'s admission :

D is given $\frac{1}{6}$th share. Hence the remaining share is $1 - \frac{1}{6} = \frac{5}{6}$

A's share $= \frac{3}{5}$ of $\frac{5}{6} = \frac{3}{6}$

B's share $= \frac{1}{5}$ of $\frac{5}{6} = \frac{1}{6}$

C's share $= \frac{1}{5}$ of $\frac{5}{6} = \frac{1}{6}$

D's share $= \frac{1}{6}$

(3) As the new profit sharing ratios are not given in the question, it will be presumed that the partners have sacrificed in their old ratio.

ILLUSTRATION 27.

A and *B* are partners sharing profits & losses as 2 : 1. *C* and *D* are admitted and profit sharing ratio becomes 4 : 2 : 3 : 1. Goodwill is valued at ₹2,00,000. *D* brings required goodwill and ₹50,000 cash for Capital. *C* brings in ₹50,000 cash and ₹40,000 worth stock as his capital in addition to the required amount of goodwill in cash.

Show the necessary journal entries.

SOLUTION:

JOURNAL ENTRIES

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c	Dr.		70,000	
	To *D*'s Capital A/c				50,000
	To Premium for Goodwill A/c				20,000
	(Amount of capital and goodwill/premium brought in cash, *i.e.*, ₹50,000 + ₹20,000[1])				
	Bank A/c	Dr.		1,10,000	
	Stock A/c	Dr.		40,000	
	To *C*'s Capital A/c				90,000
	To Premium for Goodwill A/c				60,000
	(Amount of capital and goodwill brought in cash, *i.e.*, ₹50,000 + ₹60,000[1] and stock worth ₹40,000 for capital)				
	Premium for Goodwill A/c	Dr.		80,000	
	To *A*'s Capital A/c				53,333
	To *B*'s Capital A/c				26,667
	(Amount of goodwill/premium transferred to old partners in sacrificing ratio *i.e.*, 2 : 1[2])				

Working Notes : (1) Calculation of goodwill of *D*'s share and *C*'s share :

Value of the total goodwill of the firm = ₹2,00,000

Therefore, D's share of goodwill $= ₹2,00,000 \times \frac{1}{10} = ₹20,000$

C's share of goodwill $= ₹2,00,000 \times \frac{3}{10} = ₹60,000$

(2) Calculation of Sacrificing Ratio : Sacrifice Ratio = Old Ratio – New Ratio

A's Sacrifice $= \frac{2}{3} - \frac{4}{10} = \frac{8}{30}$

B's Sacrifice $= \frac{1}{3} - \frac{2}{10} = \frac{4}{30}$

Thus Sacrifice Ratio $= \frac{8}{30} : \frac{4}{30} = 8 : 4 = 2 : 1.$

ILLUSTRATION 28.

A and *B* are partners sharing profits and losses in the ratio of 2 : 1. They admit *C* as a partner for $\frac{1}{5}$th share. *C* brings in ₹5,00,000 as his capital and his share of goodwill in cash. For this purpose, the goodwill of the firm is to be calculated at three year's purchase of the average profits of the total last four years. The profits of the last four years ending 31st March were :

Year	*Profit (₹)*	
2015-16	1,60,000	(after charging loss of ₹25,440 on sale of plant)
2016-17	1,40,000	(after charging voluntary retirement compensation of ₹50,000)
2017-18	2,50,000	
2018-19	2,40,000	

The following information is provided :

(*i*) On 1st October 2016, the firm had purchased a Computer for ₹60,000 and it was debited to stationery expenses. Depreciation is to be charged on Computer @ 20% p.a. on the Diminishing Balance Method.

(*ii*) The Closing Stock ending 31st March 2017 and 2018 were overvalued by ₹20,000 and ₹30,000 respectively.

(*iii*) To cover the operating cost, an annual charge of ₹10,000 should be made for the purpose of valuation of goodwill.

Pass necessary journal entries on admission of *C*.

SOLUTION :

Calculation of Adjusted Profits

Particulars	*2015-16*	*2016-17*	*2017-18*	*2018-19*
	₹	₹	₹	₹
Profits	1,60,000	1,40,000	2,50,000	2,40,000
Add : Loss on Sale of Plant	25,440			
Add : Voluntary Retirement Compensation		50,000		
Add : Purchase of Computer charged as an expense		60,000		
Less : Depreciation on Computer		(6,000)	(10,800)	(8,640)
Less : Overvaluation of Closing Stock		(20,000)	(30,000)	
Add : Overvaluation of Opening Stock			20,000	30,000
Less : Operating Cost	(10,000)	(10,000)	(10,000)	(10,000)
Adjusted Profits	1,75,440	2,14,000	2,19,200	2,51,360

Total Profits = ₹1,75,440 + ₹2,14,000 + ₹2,19,200 + ₹2,51,360

= ₹8,60,000

Average Profits $= 8,60,000 \div 4 =$ ₹2,15,000

Goodwill $=$ ₹2,15,000 $\times 3 =$ ₹6,45,000

C's share of Goodwill $=$ ₹6,45,000 $\times \frac{1}{5} =$ ₹1,29,000

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.		6,29,000	
	To *C*'s Capital A/c				5,00,000
	To Premium for Goodwill A/c				1,29,000
	(The amount of capital and goodwill/premium brought in cash)				
	Premium for Goodwill A/c	Dr.		1,29,000	
	To *A*'s Capital A/c				86,000
	To *B*'s Capital A/c				43,000
	(Goodwill/premium credited to old partners in their sacrificing ratio, i.e., 2 : 1)				

When Goodwill Already Appears in the Books and New Partner brings his Share of Goodwill/Premium in Cash

If new partner brings his share of goodwill in cash, and if the Goodwill Account already appears in the books of the firm, first of all the existing Goodwill Account will have to be written off. For this purpose old Partners' Capital Accounts are debited in their old profit sharing ratio and Goodwill Account is credited. Thus, the following entry is passed to write off the existing goodwill :

Old Partner's Capital A/cs   Dr.
    To Goodwill A/c
(Goodwill written off in old ratio)

ILLUSTRATION 29.

L and *M* are partners sharing profit and losses in the ratio of 4 : 3. They admit *N* for 2/7th share in the profits. *N* paid ₹30,000 for his share of goodwill. New profit sharing ratio is 3 : 2 : 2. Goodwill account appears in the books at ₹15,750. Prepare Journal entries.

SOLUTION :

JOURNAL ENTRIES

Date	Paticulars		L.F.	Dr. (₹)	Cr. (₹)
	L's Capital A/c	Dr.		9,000	
	M's Capital A/c	Dr.		6,750	
	To Goodwill A/c				15,750
	(Goodwill already appearing in the books, now written off in old ratio)				

Bank A/c Dr. To Premium for Goodwill A/c (Amount of goodwill/premium brought in cash by New Partner)		30,000	30,000
Premium for Goodwill A/c Dr. To *L*'s Capital A/c To *M*'s Capital A/c (Amount of goodwill/premium transferred to old partners in sacrificing ratio *i.e.*, 1 : 1[(1)])		30,000	15,000 15,000

Working Note : (1) Calculation of Sacrificing Ratio :

Old Ratio – New Ratio

$$L = \frac{4}{7} - \frac{3}{7} = \frac{1}{7}$$

$$M = \frac{3}{7} - \frac{2}{7} = \frac{1}{7}$$

Thus, Sacrificing Ratio = 1 : 1

(3) When the new partner does not bring his share of goodwill/premium in Cash:

Recommendation of Accounting Standard 26

Accounting Standard (AS) 26 (Intangible Assets) specifies that goodwill can be recorded in the books only when some consideration in money or money's worth has been paid for it. It means that only purchased goodwill can be recorded in the books. At the time of admission, retirement or death of a partner or in case of change in profit sharing ratio among existing partners, **goodwill account cannot be raised** in the books of the firm because it will be non-purchased goodwill (*i.e.* internally generated goodwill) and no consideration in money or money's worth has been paid for it.

When the goodwill of the firm is evaluated and the new partner does not bring his share of goodwill in cash, goodwill should be adjusted through partner's capital accounts. For this purpose **new partner's current account is debited from his share of goodwill and the old partner's capital accounts are credited in their sacrificing ratio.** Following journal entry is passed for this purpose :

New Partner's Current A/c*	Dr.	(From his share of goodwill)
To Old Partner's Capital A/cs		(In sacrificing ratio)
(Current Account of new partner debited from his share of goodwill on his admission and Capital Accounts of old partner's Credited in their sacrificing ratio)		

***Important Note :** New Partner's Current Account is debited instead of his Capital Account so that his Capital is not reduced and remains intact.

ILLUSTRATION 30.

A and *B* are partners sharing profits in the ratio of 3 : 2. They admit *C* into the partnership with $\frac{1}{4}$th share in future profits. The new profit sharing ratio is 5 : 4 : 3. *C* brings into the business ₹50,000 for his capital but could not bring any amount for

goodwill. The firm's goodwill on *C*'s admission was valued at ₹48,000. Pass journal entries.

SOLUTION :

JOURNAL ENTRIES

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.		50,000	
	To *C*'s Capital A/c				50,000
	(Amount of capital brought in cash)				
	C's Current A/c(1)	Dr.		12,000	
	To *A*'s Capital A/c				8,800
	To *B*'s Capital A/c				3,200
	(Current Account of new partner debited from his share of goodwill and Capital Accounts of old partner's credited in their sacrificing ratio *i.e.*, 11 : 4)				

Notes :

(1) Value of total goodwill of the firm $= ₹48{,}000$

C's share of goodwill $= 48{,}000 \times \frac{1}{4} = ₹12{,}000.$

(2) Calculation of Sacrificing Ratio :

Sacrifice Ratio = Old Ratio – New Ratio

$$A = \frac{3}{5} - \frac{5}{12} = \frac{36-25}{60} = \frac{11}{60}$$

$$B = \frac{2}{5} - \frac{4}{12} = \frac{24-20}{60} = \frac{4}{60}$$

Thus, Sacrifice Ratio $= \frac{11}{60} : \frac{4}{60}$ or 11 : 4

ILLUSTRATION 31.

A, B, C and *D* were partners in a firm sharing profits and losses equally. *E* was admitted as a new partner for $\frac{1}{3}$ rd share in the profits of the firm which he acquires equally from *C* and *D*. On *E*'s admission the goodwill of the firm was valued at ₹3,00,000.

Calculate the new profit sharing ratio on *E*'s admission. Also pass necessary journal entry on *E*'s admission, assuming that he failed to bring his share of goodwill in cash. *(C.B.S.E. 2019, Rajasthan)*

SOLUTION :

Calculation of New Profit Sharing Ratio :

(*a*) New Share = Old Share – Sacrifice Share

Sacrifice of *C* and *D* $= \frac{1}{2} \times \frac{1}{3} = \frac{1}{6}$ each

A's New Share $= \frac{1}{4}$

B's New Share $= \frac{1}{4}$

C's New Share $= \frac{1}{4} - \frac{1}{6} = \frac{3-2}{12} = \frac{1}{12}$

D's New Share $= \frac{1}{4} - \frac{1}{6} = \frac{3-2}{12} = \frac{1}{12}$

New ratio of A, B, C, D & E $= \frac{1}{4} : \frac{1}{4} : \frac{1}{12} : \frac{1}{12} : \frac{1}{3} = 3:3:1:1:4$

(b) **Books of *A, B, C, D* and *E***

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	E's Current A/c	Dr.		1,00,000	
	To *C*'s Capital A/c				50,000
	To *D*'s Capital A/c				50,000
	(Goodwill adjustment on *E*'s admission)				

CASE BASED MCQs — 2

Ritesh and Somesh are partners in a firm sharing profits and losses equally.

They admit Satvik on 1st April, 2021 for ⅕ share in the profits of the firm, future profit-sharing ratio between Ritesh and Somesh would be 3:2.

At the time of reconstitution of a partnership firm, goodwill was valued at two years' purchase of the average profits of the preceding four years which were as follows:

Year	*Profit/Loss*		
2017-18	Profit	₹70,000	(after debiting loss of stock by fire ₹15,000)
2018-19	Profit	₹50,000	(including insurance claim of ₹5,000)
2019-20	Loss	₹40,000	(after debiting voluntary retirement compensation paid ₹20,000)
2020-21	Profit	₹60,000	(excluding insurance premium of ₹10,000 on insurance of assets)

(*a*) **The average profits of the firm from the year 2017-18 to the year 2020-21 were:**

(*i*) ₹30,000 (*ii*) ₹60,000

(*iii*) ₹37,500 (*iv*) ₹40,000

(*b*) **The value of goodwill of the firm on Satvik's admission was:**

(*i*) ₹60,000 (*ii*) ₹ 80,000

(*iii*) ₹75,000 (*iv*) ₹1,20,000

(*c*) **Satvik is unable to bring in cash his share of goodwill. The account to be debited to record his goodwill compensation will be:**

(*i*) Satvik's Capital A/c (*ii*) Satvik's Current A/c

(*iii*) Premium for Goodwill A/c (*iv*) Old Partners' Capital A/cs

(I.S.C. Sample Paper, 2021)

(See Answers at the end of the book)

ILLUSTRATION 32.

Cake and Muffin are partners sharing profits and losses in the ratio of 5 : 4. On 1st April, 2016, they admit Cookie as a new partner for 1/6th share in the profits of the firm and the new ratio agreed upon is 3 : 2 : 1.

Goodwill, at the time of Cookie's admission is to be valued on the basis of capitalisation of the average profits of the last three years. Profits for the last three years were :

Year ended 31st March, 2014	₹39,000 (including an abnormal loss of ₹9,000).
Year ended 31st March, 2015	₹83,000 (including an abnormal gain of ₹8,000).
Year ended 31st March, 2016	₹72,000.

On 1st April, 2016, the firm had assets of ₹8,00,000. Its creditors amounted to ₹3,60,000. The firm had a Reserve Fund of ₹40,000 while Partners' Capital Accounts showed a balance of ₹4,00,000.

The normal rate of return expected from this class of business is 13%.

Cookie brings in ₹2,00,000 for her capital but is unable to bring in cash for her share of goodwill.

You are required to :

(*i*) Calculate Cookie's Share of Goodwill in the firm (Show your workings clearly).

(*ii*) Pass Journal entries at the time of Cookie's admission.

(ISC Sample Paper 2017)

SOLUTION :

(*i*) Calculation of Cookie's Share of Goodwill in the firm :

Calculation of Average Normal Profit :

Year ended	*Profit*	₹
31st March, 2014	(₹39,000 + ₹9,000)	48,000
31st March, 2015	(₹83,000 – ₹8,000)	75,000
31st March, 2016		72,000
		1,95,000

Average Normal Profit $= \dfrac{₹1,95,000}{3} = ₹65,000$

Capitalised Value of Average Profits $= \dfrac{\text{Average Normal Profit}}{\text{Normal Rate of Return}} \times 100$

$= \dfrac{₹65,000}{13} \times 100 = ₹5,00,000$

Capital Employed (Net Assets) = Total Assets – Outside Liabilities

= ₹8,00,000 – ₹3,60,000 = ₹4,40,000

Goodwill = Capitalised Value of Average Profits – Net Assets

= ₹5,00,000 – ₹4,40,000 = ₹60,000

Cookie's Share of Goodwill $= ₹60,000 \times \dfrac{1}{6} = ₹10,000.$

(*ii*) JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2016					
April 1	Bank A/c	Dr.		2,00,000	
	To Cookie's Capital A/c				2,00,000
	(Amount of capital brought in cash)				
April 1	Cookie's Current A/c	Dr.		10,000	
	To Cake's Capital A/c				3,333
	To Muffin's Capital A/c				6,667
	(Cookie's share of goodwill credited to sacrificing partners in their sacrificing ratio of 1 : 2)				

Note : Calculation of Sacrificing Ratio :

Cake's sacrifice $= \frac{5}{9} - \frac{3}{6} = \frac{10-9}{18} = \frac{1}{18}$;

Muffin's sacrifice $= \frac{4}{9} - \frac{2}{6} = \frac{8-6}{18} = \frac{2}{18}$

Sacrificing Ratio of Cake and Muffin $= \frac{1}{18} : \frac{2}{18}$ or 1 : 2.

When Goodwill Already Appears in the Books and New Partner does not bring his Share of Goodwill/Premium in Cash

If goodwill account already exists in the books of the firm, and if the new partner does not bring in his share of goodwill in cash, even then, as already discussed, the amount of goodwill already existing is written off by debiting the capital accounts of old partners in their old ratio.

ILLUSTRATION 33.

X and *Y* are partners sharing Profit & Losses in the ratio of 5 : 3. They agreed to admit *Z* into partnership for 1/8th share which he acquires equally from *X* and *Y*. His share of Goodwill is ₹12,000 but he is unable to bring it in cash. Goodwill already appears in the books at ₹40,000.

Pass necessary journal entries.

SOLUTION : JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	X's Capital A/c	Dr.		25,000	
	Y's Capital A/c	Dr.		15,000	
	To Goodwill A/c				40,000
	(Goodwill already appearing in the books, now written off in old ratio)				
	Z's Current A/c	Dr.		12,000	
	To *X*'s Capital A/c				6,000
	To *Y*'s Capital A/c				6,000
	(*Z*'s share of goodwill credited to *X* and *Y* in sacrificing ratio)				

ILLUSTRATION 34.

P and *Q* share profits in the ratio of 7 : 3. *R* is admitted for 2/7th share in profits. Goodwill already appears in the balance sheet at ₹1,00,000. Pass the necessary journal entries if :

(1) *R* cannot bring cash for his share of goodwill ₹80,000.

(2) *R* brings in cash ₹80,000 for his share of goodwill.

SOLUTION :

(1) When goodwill is not brought in Cash :

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	P's Capital A/c	Dr.		70,000	
	Q's Capital A/c	Dr.		30,000	
	To Goodwill A/c				1,00,000
	(Goodwill already appearing in the books, now written off in old ratio)				
	R's Current A/c	Dr.		80,000	
	To *P*'s Capital A/c				56,000
	To *Q*'s Capital A/c				24,000
	(*R*'s share of goodwill credited to *P* and *Q* in sacrificing ratio)				

(2) When goodwill is brought in Cash :

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	P's Capital A/c	Dr.		70,000	
	Q's Capital A/c	Dr.		30,000	
	To Goodwill A/c				1,00,000
	(Goodwill already appearing in the books, now written off in old ratio)				
	Bank A/c	Dr.		80,000	
	To Premium A/c				80,000
	(Premium for goodwill brought in cash by new partner)				
	Premium A/c	Dr.		80,000	
	To *P*'s Capital A/c				56,000
	To *Q*'s Capital A/c				24,000
	(Premium for goodwill transferred to old partners in sacrificing ratio)				

Notes 1. Goodwill already appearing in the old balance sheet is written off, by debiting the old partner's Capital Accounts in their old ratio.

2. When new profit sharing ratios are not given, the old ratios are assumed to be the sacrificing ratio.

When new partner brings in only a part of his share of goodwill/premium :

ILLUSTRATION 35.

A and *B* are partners sharing profits in the ratio of 3 : 2. They admit *C* into the firm for 1/4th share in profit which he takes 1/6th from *A* and 1/12th from *B*. *C* brings

₹50,000 as goodwill out of his share of ₹90,000. No goodwill account appears in the books of the firm. Pass necessary journal entries to record this arrangement.

SOLUTION:

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c	Dr.		50,000	
	To Premium for Goodwill A/c				50,000
	(A part of his share of goodwill/premium brought in by *C*)				
	Premium for Goodwill A/c	Dr.		50,000	
	C's Current A/c	Dr.		40,000	
	To *A*'s Capital A/c				60,000
	To *B*'s Capital A/c				30,000
	(Goodwill/premium credited to *A* and *B* in their sacrificing ratio, *i.e.*, 2 : 1)				

ILLUSTRATION 36.

A and *B* are partners sharing profits equally. They admit *C* into partnership, *C* paying only ₹60,000 for premium out of his share of premium of ₹1,08,000 for 1/4th share of profit. Goodwill account appears in the books at ₹3,00,000. All the partners have decided that goodwill should not appear in the new firm's books. Give the necessary journal entries.

SOLUTION:

JOURNAL ENTRIES

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	A's Capital A/c	Dr.		1,50,000	
	B's Capital A/c	Dr.		1,50,000	
	To Goodwill A/c				3,00,000
	(Existing goodwill written off)				
	Bank A/c	Dr.		60,000	
	To Premium for Goodwill A/c				60,000
	(A part of his share of goodwill/premium brought in by *C*)				
	Premium for Goodwill A/c	Dr.		60,000	
	C's Current A/c	Dr.		48,000	
	To *A*'s Capital A/c				54,000
	To *B*'s Capital A/c				54,000
	(Goodwill/premium credited to old partners in their sacrificing ratio, *i.e.*, 1 : 1)				

ILLUSTRATION 37.

(Sacrificing Ratio and Gaining Ratio)

A and *B* are partners sharing profits and losses in the ratio of 4 : 1. They admit *C* into partnership for $\frac{1}{6}$ th share for which he pays ₹20,000 for goodwill. *A*, *B* and *C* decide to share future profits in the ratio of 3 : 2 : 1 respectively. Give the necessary journal entries.

SOLUTION:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.		20,000	
	To Premium for Goodwill A/c				20,000
	(Premium for goodwill brought in by C for his $\frac{1}{6}$th share)				
	Premium for Goodwill A/c	Dr.		20,000	
	B's Capital A/c	Dr.		16,000	
	To A's Capital A/c				36,000
	(Premium for goodwill brought in by C credited to A alongwith $\frac{4}{30}$ of the goodwill to be contributed by B due to gain in his profit sharing ratio)				

Working Note :

Old Ratio of A and B = 4 : 1

New Ratio of A, B and C = 3 : 2 : 1

Sacrifice or Gain :

$$A \quad \frac{4}{5}-\frac{3}{6} = \frac{24-15}{30} = \frac{9}{30} \text{ (Sacrifice)}$$

$$B \quad \frac{1}{5}-\frac{2}{6} = \frac{6-10}{30} = \frac{4}{30} \text{ (Gain)}$$

$$C \quad \frac{1}{6} \text{ or } \frac{5}{30} \text{ (Gain)}$$

Only A sacrifices his share to the benefit of B and C. Consequently, not only the goodwill brought in by C will be credited to A, B must also give $\frac{4}{30}$ th share of goodwill to A. The total value of Firm's goodwill based on C's share is $20,000 \times \frac{6}{1}$ or ₹1,20,000. Hence, the amount of goodwill to be contributed by B will be (₹1,20,000 $\times \frac{4}{30}$) or ₹16,000. This will be adjusted by debiting B's Capital and Crediting A's Capital.

ILLUSTRATION 38.

(Sacrificing Ratio and Gaining Ratio)

E and F are partners sharing profits and losses in the ratio of 4 : 1 respectively. G is admitted as a partner for which he pays ₹1,00,000 as premium for goodwill and in future E, F and G decide to share profits and losses in the ratio of 2 : 1 : 1 respectively.

You are required to pass a single journal entry to give effect to the above arrangement.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.		1,00,000	
	F's Capital A/c	Dr.		20,000	
	To *E*'s Capital A/c				1,20,000
	(Premium for goodwill paid by *G* credited to the sacrificing partner *E* and further adjustment for goodwill for acquiring 1/20 share by *F* from *E*)				

Working Note :

Old Ratio of *E* and *F* = 4 : 1

New Ratio of *E*, *F* and *G* = 2 : 1 : 1

Sacrifice or Gain :

$$E \quad \frac{4}{5}-\frac{2}{4} = \frac{16-10}{20} = \frac{6}{20} \text{ (Sacrifice)}$$

$$F \quad \frac{1}{5}-\frac{1}{4} = \frac{4-5}{20} = \frac{1}{20} \text{ (Gain)}$$

$$G \quad = \frac{1}{4} \text{ or } \frac{5}{20} \text{ (Gain)}$$

Only *E* sacrifices his share to the benefit of *F* and *G*. Consequently, not only the goodwill from *G* will be credited to *E*, *F* must also give $\frac{1}{20}$ th share of goodwill to *E*. The total value of Firm's goodwill based on *G*'s share is ₹1,00,000 × $\frac{4}{1}$ or ₹4,00,000. Hence, the amount of goodwill to be contributed by *F* will be (₹4,00,000 × 1/20) or ₹20,000. This will be adjusted by debiting *F*'s Capital A/c and crediting *E*'s Capital A/c.

ILLUSTRATION 39.

A, *B* and *C* were in partnership sharing profits and losses in the ratio of 7 : 3 : 2. On 1st April, 2021, they admit *D* into partnership on the following terms :

(1) *D* to bring in ₹1,00,000 as capital.

(2) Goodwill to be valued at 80% of the average annual profits of the previous three or four years whichever is higher. *D* will bring in his share of goodwill in cash.

(3) The profits of the past years were :

Year ended 31st March	₹
2018	93,000
2019	68,000
2020	1,00,000
2021	75,000

(4) The new profit sharing ratio will be 4 : 3 : 3 : 2.

(5) The new partner is entitled to a salary of ₹500 per month. *B* personally guaranteed that the aggregate of salary and share of profit of the new partner shall not be less than ₹40,000 per annum.

Profits for the year ended 31st March 2022 amounted to ₹1,95,000 before charging *D*'s salary.

Pass necessary entries at the time of admission of the new partner and show the distribution of profits for the year ended 31st March, 2022.

SOLUTION:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2021					
April 1	Bank A/c	Dr.		1,11,200	
	To D's Capital A/c				1,00,000
	To Premium for Goodwill A/c[1]				11,200
	(Amount of Capital and premium for goodwill brought in by D)				
April 1	Premium for Goodwill A/c	Dr.		11,200	
	C's Capital A/c[2]	Dr.		5,600	
	To A's Capital A/c				16,800
	(Premium for goodwill brought in by D credited to A alongwith $\frac{1}{12}$th of goodwill to be contributed by C due to gain in his profit sharing ratio)				

Working Note :

(1) Average Profit for 3 years $= \frac{68,000 + 1,00,000 + 75,000}{3} = ₹81,000$

Average Profit for 4 years $= \frac{93,000 + 68,000 + 1,00,000 + 75,000}{4} = ₹84,000$

Since average profit for 4 years is higher, goodwill shall be valued on the basis of 4 year's average profit = 80% of ₹84,000 = ₹67,200

Premium for goodwill to be brought in by $D = \frac{2}{12} \times 67,200 = ₹11,200$

(2) Old Ratio of A, B and C = 7 : 3 : 2

New Ratio of A, B, C and D = 4 : 3 : 3 : 2

Sacrifice or Gain :

$A \quad \frac{7}{12} - \frac{4}{12} = \frac{3}{12}$ (Sacrifice)

$B \quad \frac{3}{12} - \frac{3}{12} = 0$

$C \quad \frac{2}{12} - \frac{3}{12} = \frac{1}{12}$ (Gain)

$D \quad = \frac{2}{12}$ (Gain)

Since C has also gained, he should also compensate the sacrificing partner, *i.e.*, A for acquiring $\frac{1}{12}$ share. The amount of goodwill to be contributed by C to A will be ($₹67,200 \times \frac{1}{12}$) or ₹5,600. This will be adjusted by debiting C's Capital A/c and crediting A's Capital A/c.

Distribution of Profit :

	₹
Profits before charging D's salary	1,95,000
Less : D's Salary @ ₹500 per month	6,000
	1,89,000

	A ₹	B ₹	C ₹	D ₹
Share of Profit in the ratio of 4 : 3 : 3 : 2	63,000	47,250	47,250	31,500
B has guaranteed that *D*'s share of profit including his salary will not be less than ₹40,000. But his share amounts to 31,500 + 6,000 = ₹37,500. Hence the deficiency will be borne by *B*		(–) 2,500		+ 2,500
	63,000	44,750	47,250	34,000

Revaluation of Assets and Liabilities

Whenever a new partner is admitted, it becomes necessary to revalue the assets and liabilities of the firm to their true and fair values. This is done because with the passage of time the value of certain assets might have increased while the value of certain other assets might have decreased. Thus, the actual values of various assets and liabilities may be different from the values stated in the balance sheet. New partner should not suffer because of reduction in the value of assets, nor should he be benefited by increase in the value of assets. Thus, the entire profit or loss arising from revaluation is divided between the old partners in their old profit sharing ratio.

Revaluation of assets and liabilities is done with the help of a new account called **'Revaluation Account.'** Sometimes this account is called as **'Profit & Loss Adjustment A/c'**. This account is a nominal account in nature. Therefore, if there is a loss due to revaluation, revaluation account is debited and if the revaluation results in a profit, the revaluation account is credited.

Following entries are passed for the purpose of revaluation :

(*i*) For decrease in the value of assets :
Revaluation A/c or Profit & Loss Adjustment A/c Dr.
To Assets A/c
(Decrease in the value of assets)

(*ii*) For increase in the value of assets :
Assets A/c Dr.
To Revaluation A/c or Profit & Loss Adjustment A/c
(Increase in the value of assets)

(*iii*) For increase in the value of liabilities :
Revaluation A/c or Profit & Loss Adjustment A/c Dr.
To Liabilities A/c
(Increase in the value of liabilities)

(*iv*) For decrease in the value of liabilities :
Liabilities A/c Dr.
To Revaluation A/c or Profit & Loss Adjustment A/c
(Decrease in the value of liabilities)

On the basis of above entries a Revaluation Account or P & L Adjustment A/c is prepared. If the credit side of this account is in excess, it reveals a profit and if the debit side is in excess, it will reveal a loss.

Such profit or loss will be divided between the old partners in their old profit sharing ratio. Following entries are passed for this purpose :

(*a*) When revaluation account shows profit :

Revaluation A/c Dr.

To Old Partner's Capital A/cs

(Profit on revaluation credited to Old Partner's Capital A/cs)

(*b*) Above entry is reversed when revaluation account shows loss :

Old Partner's Capital A/cs Dr.

To Revaluation A/c

(Loss on revaluation debited to Old Partner's Capital A/cs)

Proforma of Revaluation account is given below :

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Decrease in value of assets	....	By Increase in value of assets	....
To Increase in value of liabilities	....	By Decrease in value of liabilities	....
To Unrecorded liabilities	....	By Unrecorded assets	....
To Profit on Revaluation transferred to old partner's capital/ current accounts (in old ratio)	....	By Loss on Revaluation transferred to old partner's capital/ current accounts (in old ratio)	....
	....		....

ILLUSTRATION 40.

Pass journal entries to record the following transactions on the admission of a new partner :

(*i*) Stock is undervalued by 10% (Book Value of Stock ₹54,000)

(*ii*) Stock is overvalued by 10% (Book Value of Stock ₹66,000)

(*iii*) Value of Land & Building is to be increased to ₹5,00,000 (Book Value ₹4,00,000)

(*iv*) Value of Land & Building is to be increased by ₹5,00,000 (Book Value ₹4,00,000)

(*v*) A debtor whose due of ₹40,000 was written off as bad debts last year, paid ₹30,000 in full settlement.

(*vi*) An old customer, whose account was written off as bad debts has promised to pay ₹15,000 in full settlement of his account of ₹25,000.

(*vii*) A liability for claim, included in creditors for ₹20,000 is settled at ₹16,000.

(*viii*) A computer purchased on 1st October 2016 for ₹40,000 debited to Office Expenses Account is to be brought into account on 31st March 2018 charging depreciation @10% p.a. on written down value basis.

SOLUTION : JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
(*i*)	Stock A/c (Working Note 1)	Dr.		6,000	
	To Revaluation A/c				6,000
	(Increase in the value of stock)				

(ii)	Revaluation A/c (Working Note 2) Dr. To Stock A/c (Decrease in the value of stock)		6,000	6,000
(iii)	Land & Building A/c Dr. To Revaluation A/c (Increase in the value of Land & Building)		1,00,000	1,00,000
(iv)	Land & Building A/c Dr. To Revaluation A/c (Increase in the value of Land & Building)		5,00,000	5,00,000
(v)	(a) Bank A/c Dr. To Bad Debts Recovered A/c (Bad-debts recovered)		30,000	30,000
	(b) Bad Debts Recovered A/c Dr. To Revaluation A/c (Bad-debts recovered transferred to Revaluation A/c)		30,000	30,000
(vi)	Sundry Debtors A/c Dr. To Revaluation A/c (Increase in Sundry Debtors)		15,000	15,000
(vii)	Creditors A/c Dr. To Bank A/c To Revaluation A/c (Claim of ₹20,000 settled at ₹16,000)		20,000	16,000 4,000
(viii)	Office Equipment A/c (Working Note 3) Dr. To Revaluation A/c (Computer wrongly debited to office expenses brought into account)		34,200	34,200

Working Notes :

(1) Actual value of Stock $= 54,000 \times \frac{100}{90} =$ ₹60,000

Difference in Actual Value and Book Value = 60,000 – 54,000 = ₹6,000.

(2) Actual value of Stock $= 66,000 \times \frac{100}{110} =$ ₹60,000

Difference in Book Value and Actual Value = 66,000 – 60,000 = ₹6,000

(3)

Value of Computer on 1st Oct. 2016	40,000
Less : Depreciation on 31st March 2017 (for 6 months)	2,000
	38,000
Less : Depreciation on 31st March 2018 (for 1 year)	3,800
	34,200

When new partner brings the amount of goodwill/premium in cash :

ILLUSTRATION 41.

The following was the Balance Sheet of Anurag and Bhawna, who were sharing profits in the ratio of 2/3 and 1/3 as at 31st March, 2022 :—

Liabilities	₹	*Assets*	₹
Creditors	65,900	Cash	1,200

Capitals :		Sundry Debtors	9,700
Anurag	30,000	Stock	20,000
Bhawna	20,000	Plant & Machinery	35,000
		Building	50,000
	1,15,900		1,15,900

On 1st April, 2022 they agreed to admit Monika into partnership on the following terms :—

(*a*) Monika was to be given 1/3 share in profits, and was to bring ₹15,000 as capital and ₹6,000 as share of goodwill.

(*b*) That the value of stock and plant & machinery were to be reduced by 10%.

(*c*) That a provision of 5% was to be created for doubtful debts.

(*d*) That the building account was to be appreciated by 20%.

(*e*) Investments worth ₹1,400 (not mentioned in the Balance Sheet) were to be taken into account.

(*f*) That the amount of goodwill was to be withdrawn by the old partners.

Pass necessary journal entries and prepare the Revaluation A/c, Capital Accounts and the Opening Balance Sheet of the new firm.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2022					
April 1	Revaluation A/c	Dr.		5,985	
	To Stock A/c				2,000
	To Plant & Machinery A/c				3,500
	To Provision for Doubtful Debts A/c				485
	(Reduction in the value of assets and provision made for doubtful debts)				
	Building A/c	Dr.		10,000	
	Investments A/c	Dr.		1,400	
	To Revaluation A/c				11,400
	(Increase in the value of Building and investments)				
	Revaluation A/c(1)	Dr.		5,415	
	To Anurag's Capital A/c				3,610
	To Bhawna's Capital A/c				1,805
	(Transfer of profit on revaluation to the capital accounts of old partners in old ratio)				
	Cash A/c	Dr.		21,000	
	To Monika's Capital A/c				15,000
	To Premium for Goodwill A/c				6,000
	(Amount of capital and premium for goodwill brought in cash by Monika)				

Premium for Goodwill A/c Dr.		6,000	
To Anurag's Capital A/c			4,000
To Bhawna's Capital A/c			2,000
(Premium for goodwill credited to old partners in the sacrificing ratio 2 : 1)			
Anurag's Capital A/c Dr.		4,000	
Bhawna's Capital A/c Dr.		2,000	
To Cash A/c			6,000
(Premium for goodwill withdrawn by old partners)			

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Stock A/c		2,000	By Building A/c	10,000
To Plant & Machinery A/c		3,500	By Investments A/c	1,400
To Provision for Doubtful debts A/c		485		
To Profit Transferred to Capital Accounts :				
Anurag	3,610			
Bhawna	1,805	5,415		
		11,400		11,400

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*Anurag*	*Bhawna*	*Monika*	*Particulars*	*Anurag*	*Bhawna*	*Monika*
	₹	₹	₹		₹	₹	₹
To Cash A/c	4,000	2,000	—	By Balance b/d	30,000	20,000	—
To Balance c/d	33,610	21,805	15,000	By Revaluation A/c	3,610	1,805	—
				By Cash A/c	—	—	15,000
				By Premium for goodwill A/c	4,000	2,000	—
	37,610	23,805	15,000		37,610	23,805	15,000

OPENING BALANCE SHEET

as at 1st April, 2022

Liabilities		₹	*Assets*		₹
Sundry Creditors		65,900	Cash in Hand[(2)]		16,200
Capitals :			Sundry Debtors	9,700	
Anurag	33,610		*Less* : Provision	485	9,215
Bhawna	21,805		Stock		18,000
Monika	15,000	70,415	Investments		1,400
			Plant & Machinery		31,500
			Building		60,000
		1,36,315			1,36,315

Notes: 1. Profit or Loss on revaluation is always divided between the old partners in their old profit sharing ratios.

2. Calculation of Cash Balance :—

	₹
Opening Balance	1,200
(+) Amount of Goodwill brought in by the new partner in Cash	6,000
(+) Amount of Capital brought in by the new partner in Cash	15,000
	22,200
(–) Amount of Goodwill withdrawn by the old partners in Cash	6,000
Balance	16,200

Accounting Treatment of Reserves and Accumulated Profits or Losses

At the time of admission, if there is any General Reserve, Reserve Fund or the balance of Profit and Loss Account appearing in the balance sheet, it must be transferred to Old Partner's Capital Accounts in their old profit sharing ratio. The new partner is not entitled to any share of such reserves or profits, as these are undistributed profits earned by the old partners. For this purpose, the following journal entries are recorded :

(*i*) For distributing Reserves and Accumulated Profits :

General Reserve A/c Dr.
Reserve Fund A/c Dr.
Profit & Loss A/c (Credit balance) Dr.
To Old Partner's Capital A/cs or Current A/cs

(*ii*) For distributing accumulated losses among old partners in old ratio :

If there is any accumulated loss like debit balance of Profit & Loss A/c, Advertisement Suspense A/c, Deferred Revenue Expenditure etc. it should be debited to Old Partner's Capital Accounts in their old profit sharing ratio. The entry will be :

Old Partner's Capital A/cs or Current A/cs Dr.
To Profit & Loss A/c (Debit balance)
To Advertisement Suspense A/c
To Deferred Revenue Expenditure A/c

(*iii*) For distributing surplus of specific reserves :

The firm may have created some specific reserves like 'Workmen's Compensation Reserve' or 'Investment Fluctuation Reserve' to meet certain future obligations. At the time of admission of a new partner, such reserves may be in excess of actual obligations. Such excess reserves will be transferred to capital accounts of old partners in old ratio. The entry will be :

Workmen's Compensation Reserve A/c Dr.
Investment Fluctuation Reserve A/c Dr.
To Old Partner's Capital A/cs or Current A/cs

Entries for transferring the Reserves and Accumulated Profits or Losses must be passed even if the question is silent on this point.

Employee's Provident Fund or Employee's Saving Account appearing on the Liabilities side of the Balance Sheet are not distributed among old partners as they are not reserves but are the outside liabilities payable by the firm.

ILLUSTRATION 42.

(Reserves and Accumulated Profits)

Leela and Meeta were partners in a firm sharing profits and losses in the ratio of 5 : 3. On 1st April, 2022 they admitted Om as a new partner. On the date of Om's admission the balance sheet of Leela and Meeta showed a balance of ₹1,60,000 in General reserve and ₹2,40,000 (Cr) in Profit and Loss Account. Record necessary journal entries for the treatment of these items on Om's admission. The new profit sharing ratio between Leela, Meeta and Om was 5 : 3 : 2.

SOLUTION :

Books of Leela, Meeta and Om

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
April 1	General Reserve A/c	Dr.		1,60,000	
	To Leela's Capital A/c				1,00,000
	To Meeta's Capital A/c				60,000
	(The transfer of the balance of General Reserve to old partner's capital accounts in old ratio on the admission of Om)				
April 1	Profit & Loss A/c	Dr.		2,40,000	
	To Leela's Capital A/c				1,50,000
	To Meeta's Capital A/c				90,000
	(The transfer of the balance of Accumulated Profits to old partner's capital accounts in old ratio on the admission of Om)				

ILLUSTRATION 43.

Ram and Mohan were partners in a firm sharing profits in the ratio of 4 : 1. On 1-3-2022, they admitted Sohan as a new partner for 1/3rd share in the profits of the firm. They fixed the new profit sharing ratio as 4 : 2 : 3.

The P & L A/c on the date of admission showed a Balance of ₹32,000 (Dr.). The firm also had a reserve of ₹1,00,000. Sohan is to bring ₹60,000 as premium for his share of goodwill.

Showing your calculations clearly, pass necessary journal entries to record the above transactions.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
1-3-22	Ram Capital A/c	Dr.		25,600	
	Mohan's Capital A/c	Dr.		6,400	
	To Profit & Loss A/c				32,000
	(Accumulated loss transferred to old partner's capital accounts on the admission of Sohan)				

1-3-22	Reserve A/c Dr. To Ram's Capital A/c To Mohan's Capital A/c (Reserve transferred to old partner's capital accounts on the admission of Sohan)		1,00,000	 80,000 20,000
1-3-22	Bank A/c Dr. To Premium for Goodwill A/c (Premium for goodwill brought in by Sohan for 1/3rd share)		60,000	 60,000
1-3-22	Premium for Goodwill A/c Dr. Mohan's Capital A/c Dr. To Ram's Capital A/c (Premium for goodwill brought in by Sohan credited to Ram along with $\frac{1}{45}$ of the goodwill to be contributed by Mohan due to gain in his profit sharing ratio)		60,000 4,000	 64,000

Working Note :

Old Ratio of Ram and Mohan = 4 : 1

New Ratio of Ram, Mohan and Sohan = 4 : 2 : 3

Sacrifice or Gain :

Ram $= \frac{4}{5} - \frac{4}{9} = \frac{36-20}{45} = \frac{16}{45}$ (Sacrifice)

Mohan $= \frac{1}{5} - \frac{2}{9} = \frac{9-10}{45} = \frac{1}{45}$ (Gain)

Sohan $= \frac{3}{9}$ or $\frac{15}{45}$ (Gain)

Since Mohan is gaining 1/45 in the profit, therefore, he will also compensate Ram proportionately :

For 1/3rd share Sohan brought ₹60,000 as premium. Therefore, Mohan will compensate Ram by ₹60,000 × 3/1 × 1/45 = ₹4,000.

Workmen Compensation Reserve :

This reserve is created out of firm's profits to pay compensation to employees. At the time of admission of a partner, it is treated as follows :

(1) **If there is no claim against Workmen Compensation Reserve :** In such a case, the entire amount of Workmen Compensation Reserve is credited to the Capital Accounts of old partners in their old profit sharing ratio :

The Journal Entry passed is :
Workmen Compensation Reserve A/c Dr.
To Partner's Capital A/cs
(Workmen Compensation Reserve credited to old partners Capital Accounts in their old profit sharing ratio)

(2) **If the claim for workmen compensation is lower than the amount of Workmen Compensation Reserve :** The amount of claim is credited to

'Provision for Workmen Compensation Claim A/c' and balance is credited to the Capital Accounts of old partners in their old profit sharing ratio (Suppose Workmen Compensation Reserve is ₹50,000 and liability for claim is ₹20,000). The Journal Entry passed is :

Workmen Compensation Reserve A/c	Dr.	50,000	
To Provision for Workmen Compensation Claim A/c			20,000
To Partner's Capital A/cs			30,000
(Amount of claim transferred to liability and balance to partner's Capital Accounts in their old profit sharing ratio)			

(3) **If the claim is equal to Workmen Compensation Reserve :** Entire amount of Workmen Compensation Reserve is transferred to Provision for Workmen Compensation Claim A/c :

Workmen Compensation Reserve A/c	Dr.		
To Provision for Workmen Compensation Claim A/c			
(Provision made for Workmen Compensation Claim)			

(4) **If the claim is more than the amount of Workmen Compensation Reserve:** Entire amount of Workmen Compensation Reserve along with the excess claim is credited to 'Provision for Workmen Compensation Claim A/c'. The amount of excess claim is debited to 'Revaluation Account' because the loss must be borne by all of the old partners in their old profit sharing ratio. (Suppose Workmen Compensation Reserve is ₹50,000 and liability for claim is ₹60,000). The Journal Entries passed are :

(*i*) Workmen Compensation Reserve A/c	Dr.	50,000	
Revaluation A/c	Dr.	10,000	
To Provision for Workmen Compensation Claim A/c			60,000
(Amount of claim debited to Workmen Compensation Reserve and Revaluation A/c)			
(*ii*) Partner's Capital A/cs	Dr.	10,000	
To Revaluation A/c			10,000
(Loss on revaluation transferred to capital accounts of old partners in their old profit sharing ratio)			

ILLUSTRATION 44.

A, *B* and *C* are partners sharing profits and losses in the ratio of 2 : 2 : 1. They admitted *D* for 1/4th share with effect from 1st April, 2022. An extract of their Balance Sheet as at 31st March, 2022 is as follows :

Liabilities	₹	*Assets*	₹
Workmen Compensation Reserve	80,000		

Show the accounting treatment under the following alternative cases :

Case 1. If there is no other information.

Case 2. If a claim for workmen compensation is estimated at ₹50,000.

Case 3. If a claim for workmen compensation is estimated at ₹80,000.

Case 4. If a claim for workmen compensation is estimated at ₹1,00,000.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
April 1 Case 1	Workmen Compensation Reserve A/c	Dr.		80,000	
	To *A*'s Capital A/c				32,000
	To *B*'s Capital A/c				32,000
	To *C*'s Capital A/c				16,000
	(Workmen Compensation Reserve credited to old Partners' Capital Accounts in their old profit-sharing ratio)				
Case 2	Workmen Compensation Reserve A/c	Dr.		80,000	
	To Provision for Workmen Compensation Claim A/c				50,000
	To *A*'s Capital A/c				12,000
	To *B*'s Capital A/c				12,000
	To *C*'s Capital A/c				6,000
	(Surplus workmen compensation reserve credited to old Partners' Capital Accounts in their old profit-sharing ratio)				
Case 3	Workmen Compensation Reserve A/c	Dr.		80,000	
	To Provision for Workmen Compensation Claim A/c				80,000
	(Provision made for Workmen Compensation Claim)				
Case 4	Workmen Compensation Reserve A/c	Dr.		80,000	
	Revaluation A/c	Dr.		20,000	
	To Provision for Workmen Compensation Claim A/c				1,00,000
	(Provision made for workmen claim and shortfall charged to Revaluation Account)				
	A's Capital A/c	Dr.		8,000	
	B's Capital A/c	Dr.		8,000	
	C's Capital A/c	Dr.		4,000	
	To Revaluation A/c				20,000
	(Loss on revaluation debited to Partners' Capital Accounts in their old profit-sharing ratio)				

ILLUSTRATION 45.

P and *Q* are partners sharing profits in the ratio of 3 : 2. They admitted *R* for 1/4th share. On this date, General Reserve appeared in the books at ₹1,00,000 out of which 25% is to be retained as 'Provision for Workmen Compensation Claim'. Record necessary journal entry.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	General Reserve A/c	Dr.		1,00,000	
	To Provision for Workmen Compensation Claim A/c				25,000
	To *P*'s Capital A/c				45,000
	To *Q*'s Capital A/c				30,000
	(25% of General Reserve transferred to Workmen Compensation Claim A/c and balance transferred to old partners in their old profit-sharing ratio)				

ILLUSTRATION 46.

Krishna and Suresh were partners in a firm sharing profits in the ratio of 3 : 1. On 1st April, 2015 they admitted Rahul as a new partner for 1/5th share in profits of the firm. On the date of Rahul's admission the Balance Sheet of Krishna and Suresh showed a General Reserve of ₹1,20,000, a debit balance of ₹60,000 in Profit and Loss A/c and Workmen Compensation Reserve of ₹1,50,000.

The following was agreed upon on Rahul's admission :

(*i*) Rahul will bring ₹1,50,000 as his capital and his share of goodwill premium in cash.

(*ii*) Goodwill of the firm be valued at ₹2,40,000.

(*iii*) There was a claim of Workmen Compensation for ₹1,70,000.

(*iv*) The partners decided to share future profits in the ratio of 3 : 1 : 1.

Pass the necessary Journal entries for the above on Rahul's admission.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2015					
April 1	General Reserve A/c	Dr.		1,20,000	
	To Krishna's Capital A/c				90,000
	To Suresh's Capital A/c				30,000
	(General Reserve distributed between the old partners in their old ratio of 3 : 1)				
	Krishna's Capital A/c	Dr.		45,000	
	Suresh's Capital A/c	Dr.		15,000	
	To Profit and Loss A/c				60,000
	(Loss distributed between the old partners in their old ratio of 3 : 1)				
	Workmen Compensation Reserve A/c	Dr.		1,50,000	
	Revaluation A/c	Dr.		20,000	
	To Provision for Workmen Compensation Claim A/c				1,70,000
	(Adjustment of claim against Workmen Compensation Reserve)				
	Krishna's Capital A/c	Dr.		15,000	
	Suresh's Capital A/c	Dr.		5,000	
	To Revaluation A/c				20,000
	(Transfer of loss on revaluation in old ratio of 3 : 1)				
	Bank A/c	Dr.		1,98,000	
	To Rahul's Capital A/c				1,50,000
	To Premium for Goodwill A/c (₹2,40,000 × 1/5)				48,000
	(Cash brought in by Rahul)				

	Premium for Goodwill A/c Dr.		48,000	
	To Krishna's Capital A/c			36,000
	To Suresh's Capital A/c			12,000
	(Premium for goodwill credited in sacrificing ratio of 3 : 1)			

Investment Fluctuation Reserve :

This reserve is created out of firm's profits to meet the fall in the market value of investments. At the time of admission of a partner, this reserve is treated as follows :

1. **When Book Value and Market Value of Investments is same :** In such a case, the entire amount of Investment Fluctuation Reserve is transferred to the Capital Accounts of **old partners** in their **old profit sharing ratio.** The entry is :

   Investment Fluctuation Reserve A/c Dr.
   To Partner's Capital A/cs

2. **When Market Value of Investments is less than the Book Value :** In such a case, the accounting treatment depends on the quantum of decrease. There may be three possibilities :

   (*i*) **Fall in the value is less than Investment Fluctuation Reserve :** In such a case, Investment Fluctuation Reserve, to the extent of fall in value, is credited to Investments A/c and the balance is credited to old Partner's Capital A/cs in their old profit sharing ratio. The entry is :

   Investment Fluctuation Reserve A/c Dr.
   To Investments A/c (Book value – Market value)
   To Partners Capital A/cs (In old ratio)

   (*ii*) **Fall in the value is Equal to Investment Fluctuation Reserve :** In such a case, entire amount of Investment Fluctuation Reserve is credited to Investments A/c. The entry is :

   Investment Fluctuation Reserve A/c Dr.
   To Investments A/c

   (*iii*) **Fall in the value is More than Investment Fluctuation Reserve :** In such a case, entire amount of Investment Fluctuation Reserve, along with the amount of excess fall in value is credited to Investments A/c. The amount of excess fall is debited to Revaluation A/c because the loss must be borne by the old partners in their old profit sharing ratio. The entry is :
   Investment Fluctuation Reserve A/c Dr.
   Revaluation A/c Dr.
   To Investments A/c

3. **When Market Value of Investments is More than the Book value :** In such a case three entries are passed :

   (*i*) Entire amount of Investment Fluctuation Reserve is credited to old Partner's Capital A/cs :
   Investment Fluctuation Reserve A/c Dr.

To Partner's Capital A/cs (In old ratio)

(*ii*) Increase in the value of Investments is debited to Investments A/c and credited to Revaluation A/c :

Investments A/c Dr.
To Revaluation A/c
(To bring up the value of Investments to Market value.)

(*iii*) Revaluation A/c Dr.
To Partner's Capital A/cs
(In old ratio)

ILLUSTRATION 47.

A, B and *C* sharing profits and losses in the ratio of 3 : 2 : 1 decide to admit *D* for 1/5th share with effect from 1st April, 2022. An extract of their Balance Sheet as at 31st March, 2022 is :

Liabilities	₹	*Assets*	₹
Investments Fluctuation Reserve	30,000	Investments (At cost)	5,00,000

Show the accounting treatment under the following alternative cases :

Case 1. If there is no other information.

Case 2. If the market value of investments is ₹5,00,000.

Case 3. If the market value of investments is ₹4,82,000.

Case 4. If the market value of investments is ₹4,55,000.

Case 5. If the market value of investments is ₹5,24,000.

SOLUTION : JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2022					
April 1					
Case 1	Investments Fluctuation Reserve A/c	Dr.		30,000	
	To *A*'s Capital A/c				15,000
	To *B*'s Capital A/c				10,000
	To *C*'s Capital A/c				5,000
	(Investments fluctuation reserve credited to Partners' Capital Accounts in their old profit-sharing ratio)				
Case 2	Same entry as given in Case 1.				
Case 3	Investments Fluctuation Reserve A/c	Dr.		30,000	
	To Investments A/c				18,000
	To *A*'s Capital A/c				6,000
	To *B*'s Capital A/c				4,000
	To *C*'s Capital A/c				2,000
	(Excess investments fluctuation reserve credited to Partners' Capital Accounts in their old profit-sharing ratio)				

Case 4	Investments Fluctuation Reserve A/c	Dr.	30,000	
	Revaluation A/c	Dr.	15,000	
	To Investments A/c			45,000
	(Fall in book value of investments credited to investments account and excess fall charged to Revaluation Account)			
	A's Capital A/c	Dr.	7,500	
	B's Capital A/c	Dr.	5,000	
	C's Capital A/c	Dr.	2,500	
	To Revaluation A/c			15,000
	(Loss on revaluation debited to partners' Capital Accounts in their old profit-sharing ratio)			
Case 5	Investments Fluctuation Reserve A/c	Dr.	30,000	
	To *A*'s Capital A/c			15,000
	To *B*'s Capital A/c			10,000
	To *C*'s Capital A/c			5,000
	(Investments fluctuation reserve credited to Partners' Capital Accounts in their old profit-sharing ratio)			
	Investments A/c	Dr.	24,000	
	To Revaluation A/c			24,000
	(Value of investments brought up to market value)			
	Revaluation A/c	Dr.	24,000	
	To *A*'s Capital A/c			12,000
	To *B*'s Capital A/c			8,000
	To *C*'s Capital A/c			4,000
	(Profit on revaluation credited to partner's Capital Accounts in their old profit-sharing ratio)			

ILLUSTRATION 48.

Anil and Beena were partners in a firm sharing profits in the ratio of 4 : 3. On 1st April, 2022 they admitted Chahat as a new partner for 1/4th share in the profits of the firm. On the date of Chahat's admission, the Balance Sheet of Anil and Beena showed a General Reserve of ₹70,000, a debit balance of ₹7,000 in the Profit and Loss Account and an Investment Fluctuation Reserve of ₹10,000.

The following was agreed upon, on Chahat's admission :

(*a*) Chahat will bring ₹80,000 as her capital and her share of goodwill premium of ₹21,000 in cash.

(*b*) The market value of investments was ₹17,000 less than the book value.

(*c*) New profit-sharing ratio was agreed at 2 : 1 : 1.

Pass the necessary Journal entries for the above on Chahat's admission.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022 April 1	General Reserve A/c	Dr.		70,000	
	To Anil's Capital A/c				40,000
	To Beena's Capital A/c				30,000
	(General Reserve distributed between the old partners in their old ratio of 4 : 3)				
	Anil's Capital A/c	Dr.		4,000	
	Beena's Capital A/c	Dr.		3,000	
	To Profit and Loss A/c				7,000
	(Loss distributed between the old partners in their old ratio of 4 : 3)				
	Investment Fluctuation Reserve A/c	Dr.		10,000	
	Revaluation A/c	Dr.		7,000	
	To Investments A/c				17,000
	(Value of investments brought down to market value)				
	Anil's Capital A/c	Dr.		4,000	
	Beena's Capital A/c	Dr.		3,000	
	To Revaluation A/c				7,000
	(Transfer of loss on revaluation in old ratio of 4 : 3)				
	Bank A/c	Dr.		1,01,000	
	To Chahat's Capital A/c				80,000
	To Premium for Goodwill A/c				21,000
	(Cash brought in by Chahat)				
	Premium for Goodwill A/c	Dr.		21,000	
	To Anil's Capital A/c				6,000
	To Beena's Capital A/c				15,000
	(Premium transferred in sacrificing ratio, i.e., 2 : 5)				

Working Note :

Calculation of sacrificing ratio :

Sacrificing Ratio = Old share – New share

Anil's sacrifice $= \frac{4}{7} - \frac{2}{4} = \frac{16-14}{28} = \frac{2}{28};$

Beena's sacrifice $= \frac{3}{7} - \frac{1}{4} = \frac{12-7}{28} = \frac{5}{28}$

Sacrificing Ratio $= \frac{2}{28} : \frac{5}{28} = 2 : 5.$

ILLUSTRATION 49.

X and *Y* were partners in a firm sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as at 31st March, 2021 was as follows :

Liabilities		₹	*Assets*	₹
Creditors		42,000	Current Assets	2,00,000
Employee's Provident Fund		20,000	Investments	50,000
Contingency Reserve		30,000	Furniture	20,000
Profit & Loss Account		45,000	Machinery	90,000
Workmen Compensation Reserve		18,000	Advertisement Expenditure	
Investment Fluctuation Reserve		25,000	(Deferred Revenue	
Capitals : *X*	1,20,000		Expenditure)	20,000
Y	80,000	2,00,000		
		3,80,000		3,80,000

They admit *Z* into partnership on 1st April, 2021 and the new profit sharing ratio is agreed at 2 : 1 : 1. It is estimated that :

(*i*) Claim on account of Workmen's Compensation is estimated at ₹10,000.

(*ii*) Market value of Investments is ₹46,000.

Give necessary journal entries to adjust accumulated profits and losses.

SOLUTION:

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2021					
April 1	Investment Fluctuation Reserve	Dr.		25,000	
	To Investments A/c				4,000
	To *X*'s Capital A/c				12,600
	To *Y*'s Capital A/c				8,400
	(Excess Investment Fluctuation Reserve Credited to Partner's Capital Accounts in old ratio *i.e.* 3 : 2)				
	Workmen Compensation Reserve A/c	Dr.		18,000	
	To Provision for Workmen Compensation Claim A/c				10,000
	To *X*'s Capital A/c				4,800
	To *Y*'s Capital A/c				3,200
	(Excess Workmen Compensation Reserve Credited to Partner's Capital Accounts in old ratio *i.e.* 3 : 2)				
	Contingency Reserve A/c	Dr.		30,000	
	Profit & Loss A/c	Dr.		45,000	
	To *X*'s Capital A/c				45,000
	To *Y*'s Capital A/c				30,000
	(Transfer of accumulated profits to old partners in their old profit sharing ratio)				

X's Capital A/c	Dr.	12,000	
Y's Capital A/c	Dr.	8,000	
To Advertisement Expenditure A/c			20,000
(Transfer of accumulated loss to old partners in their old profit sharing ratio)			

Working Note : Employee's Provident Fund is outside liability payable by the firm.

CASE BASED MCQs — 3

Dhruv and Ansh are partners in a firm sharing profits and losses: Dhruv 75% and Ansh 25%. Their Balance Sheet as at 31st March, 2021 is given below:

Balance Sheet of Dhruv and Ansh

As at 31st March, 2021

Liabilities		₹	*Assets*		₹
Sundry Creditors		49,000	Cash		62,000
Workmen Comp. Reserve		5,000	Sundry Debtors	18,500	
Capital A/c:			*Less:* Prov. for		
Dhruv	30,000		Doubtful Debts	(1,500)	17,000
Ansh	20,000	50,000	Land and Building		25,000
		1,04,000			1,04,000

On 1st April 2021, Kavi is admitted as a new partner on the following terms:

(*i*) Land and building is found to be valued at 25% above cost. It is decided to bring it to its cost.

(*ii*) Bad debts amounting to ₹1,800 are to be written off. The remaining debtors are good.

(*iii*) Creditors include an amount of ₹5,000 received as commission from Amar. The necessary adjustment is required to be made.

(*iv*) The liability on Workmen Compensation Reserve is determined at ₹3,000.

(*v*) Kavi is to pay ₹15,000 to the existing partners as premium for Goodwill for 20% of the future profits of the firm. He is also to bring in ₹25,000 as capital.

(*a*) **At the time of Kavi's admission, the Workmen Compensation Reserve of:**

(*i*) ₹5,000 will be credited to the capital accounts of all the partners

(*ii*) ₹3,000 will be credited to the capital accounts of all the partners.

(*iii*) ₹2,000 will be credited to the capital accounts of the old partners.

(*iv*) ₹2,000 will be debited to the capital accounts of the old partners.

(*b*) **The value of Land & Building in the Balance Sheet of the reconstituted firm will be:**

(*i*) ₹20,000 (*ii*) ₹31,250

(*iii*) ₹ 5,000 (*iv*) ₹ 6,250

(*c*) **To adjust the creditors in adjustment (iii):**

(*i*) Commission A/c will be credited with ₹5,000.

(*ii*) Creditors A/c will be credited with ₹5,000.

(*iii*) Amar's A/c will be debited with ₹5,000.
(*iv*) Creditors A/c will be debited with ₹5,000.

(*d*) **The provision for Doubtful Debts in the reconstituted firm will be:**

(*i*) ₹1,500 (*ii*) ₹1,800
(*iii*) Nil (*iv*) None of the above

(*e*) **The date of the Balance Sheet of the reconstituted firm will be:**

(*i*) Balance Sheet for the year ending 31st March, 2022.
(*ii*) Balance Sheet as at 31st March, 2021.
(*iii*) Balance Sheet for the year ending 1st April, 2021.
(*iv*) Balance Sheet as at 1st April, 2021. *(I.S.C. Sample Paper, 2021)*

(See Answers at the end of the book)

ILLUSTRATION 50.

X and *Y* are in partnership sharing profits and losses in the ratio of 3 : 2. Their balance sheet as at 31st March, 2022, was as under :

Liabilities	₹	*Assets*		₹
Creditors	15,000	Cash		5,000
General Reserve	12,000	Debtors	20,000	
Capital Accounts :		*Less* : Provision	800	19,200
X	60,000	Patents		14,800
Y	30,000	Investments		8,000
Current Accounts :		Fixed Assets		72,000
X	10,000	Goodwill		10,000
Y	2,000			
	1,29,000			1,29,000

They admit *Z* on 1st April, 2022 on the following terms :

1. A provision of 5% is to be maintained on Debtors.
2. Accrued Income of ₹1,500 does not appear in the books and ₹5,000 are outstanding for salaries.
3. Present market value of Investments is ₹6,000. *X* takes over the Investments at this value.
4. New profit sharing ratio of partners will be 4 : 3 : 2. *Z* will bring in ₹20,000 as his capital.
5. *Z* is to pay in cash an amount equal to his share in firm's goodwill valued at twice the average profits of the last 3 years which were ₹30,000; ₹26,000 and ₹25,000 respectively.
6. Half the amount of goodwill is withdrawn by old partners.

You are required to pass Journal entries, prepare Revaluation A/c, Capital A/cs, Current A/cs and the opening Balance Sheet of the new firm.

SOLUTION:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
April 1	General Reserve A/c	Dr.		12,000	
	To *X*'s Current A/c[1]				7,200
	To *Y*'s Current A/c				4,800
	(Transfer of General Reserve to old partners current accounts)				
	Revaluation A/c	Dr.		5,200	
	To Provision for Doubtful Debts A/c				200
	To Outstanding Salaries A/c				5,000
	(Provision for doubtful debts and outstanding salaries)				
	Accrued Income A/c	Dr.		1,500	
	To Revaluation A/c				1,500
	(Accrued income)				
	X's Current A/c	Dr.		6,000	
	Revaluation A/c	Dr.		2,000	
	To Investments A/c				8,000
	(Investments taken over by *X* at revised value)				
	X's Current A/c	Dr.		3,420	
	Y's Current A/c	Dr.		2,280	
	To Revaluation A/c				5,700
	(Loss on revaluation transferred to old partners)				
	X's Current A/c[2]	Dr.		6,000	
	Y's Current A/c	Dr.		4,000	
	To Goodwill A/c				10,000
	(Goodwill already existing in the books written off in the old ratio)				
	Cash A/c[3]	Dr.		32,000	
	To *Z*'s Capital A/c				20,000
	To Premium for Goodwill A/c				12,000
	(*Z* brings in ₹20,000 for his capital and ₹12,000 as premium for goodwill)				
	Premium for Goodwill A/c	Dr.		12,000	
	To *X*'s Current A/c[4]				8,400
	To *Y*'s Current A/c				3,600
	(Premium for goodwill shared by old partners in their sacrificing ratio *i.e.*, 7 : 3)				
	X's Current A/c	Dr.		4,200	
	Y's Current A/c	Dr.		1,800	
	To Cash A/c				6,000
	(Half the amount of premium for goodwill withdrawn)				

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	Particulars		₹
To Provision for Doubtful Debts	200	By Accrued Income		1,500
To Outstanding Salaries	5,000	By Loss transferred to :		
To Investments	2,000	*X*'s Current A/c 3/5	3,420	
		Y's Current A/c 2/5	2,280	5,700
	7,200			7,200

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*X*	*Y*	*Z*	Particulars	*X*	*Y*	*Z*
	₹	₹	₹		₹	₹	₹
To Balance c/d	60,000	30,000	20,000	By Balance b/d	60,000	30,000	
				By Cash A/c			20,000
	60,000	30,000	20,000		60,000	30,000	20,000

Dr. CURRENT ACCOUNTS Cr.

Particulars	*X*	*Y*	Particulars	*X*	*Y*
	₹	₹		₹	₹
To Investments	6,000		By Balance b/d	10,000	2,000
To Revaluation	3,420	2,280	By General Reserve	7,200	4,800
To Goodwill	6,000	4,000	By Premium for		
To Cash	4,200	1,800	Goodwill A/c	8,400	3,600
To Balance c/d	5,980	2,320			
	25,600	10,400		25,600	10,400

BALANCE SHEET
as at 1st April, 2022

Liabilities	₹	Assets		₹
Creditors	15,000	Cash		31,000
Outstanding Salaries	5,000	Debtors	20,000	
Capital Accounts :		*Less* : Provision	1,000	19,000
X	60,000	Patents		14,800
Y	30,000	Fixed Assets		72,000
Z	20,000	Accrued Income		1,500
Current Accounts :				
X	5,980			
Y	2,320			
	1,38,300			1,38,300

Notes: 1. As there are Current Account balances appearing in the balance sheet, it means that the capital accounts are fixed. Hence all transactions relating to Capitals Accounts will be passed through the Current Accounts in this question.

2. The amount of goodwill already appearing in the balance sheet is written off by the old partners in their old profit sharing ratio.

3. Calculation of Goodwill : $\frac{30,000 + 26,000 + 25,000}{3}$ = ₹27,000

Goodwill = 27,000 × 2 = ₹54,000
Z brings in his share of goodwill in cash. Therefore, the amount of goodwill brought in by Z = 54,000 × $\frac{2}{9}$ = ₹12,000

4. Sacrificing Ratios :
$X\ \frac{3}{5} - \frac{4}{9} = \frac{7}{45}$ $\quad Y\ \frac{2}{5} - \frac{3}{9} = \frac{3}{45}$ $\quad$ OR 7 : 3

ILLUSTRATION 51.

A and *B* share the profits of a business in the ratio of 5 : 3. They admit *C* into the firm for 1/4th share in the profits to be contributed equally by *A* and *B*. On the date of admission of *C*, the Balance Sheet of the firm was as follows :

Liabilities	₹	*Assets*	₹
A's Capital	40,000	Machinery	30,000
B's Capital	30,000	Furniture	20,000
Workmen's Compensation Reserve	4,000	Stock	15,000
Creditors	2,000	Debtors	15,000
Provident Fund	10,000	Bank	6,000
	86,000		86,000

Terms of *C*'s admission were as follows :

(*i*) *C* will bring ₹30,000 for his share of capital and goodwill.

(*ii*) Goodwill of the firm has been valued at 3 years' purchase of the average super profits of last four years. Average profits of the last four years are ₹20,000 while the normal profits that can be earned with the capital employed are ₹12,000.

(*iii*) Furniture is undervalued by ₹12,000 and the value of stock is reduced to ₹13,000. Provident Fund be raised by ₹1,000.

(*iv*) Creditors are unrecorded to the extent of ₹6,000.

Prepare Revaluation Account, Partners' Capital Accounts and the new Balance Sheet of *A*, *B* and *C*.

SOLUTION :

Dr. REVALUATION A/C Cr.

Particulars		₹	*Particulars*	₹
To Stock A/c		2,000	By Furniture A/c	12,000
To Provident Fund A/c		1,000		
To Creditors		6,000		
To Profit transferred to				
A's Capital A/c	1,875			
B's Capital A/c	1,125	3,000		
		12,000		12,000

Calculation of Goodwill :

Super Profits = Average Profits – Normal Profits
= ₹20,000 – ₹12,000 = ₹8,000

Goodwill = Super Profits × No. of years purchased
= ₹8,000 × 3 = ₹24,000.

C brings in his share of goodwill in cash. Therefore, he brings in ₹24,000 × 1/4 = ₹6,000 for goodwill which is included in the total amount of ₹30,000 brought by him. This amount of ₹6,000 will be divided between *A* and *B* equally, because they have sacrificed in equal proportions.

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Balance c/d	47,375	35,625	24,000	By Balance b/d	40,000	30,000	
				By Workmen's Compensation Reserve	2,500	1,500(1)	
				By Revaluation A/c	1,875	1,125	
				By Bank A/c			24,000
				By Premium for Goodwill A/c	3,000	3,000	
	47,375	35,625	24,000		47,375	35,625	24,000

Note 1. Since there is no specific liability related to Workmen's Compensation Reserve it is divided in old partners in their old profit sharing ratios.

OPENING BALANCE SHEET

as at ....

Liabilities	₹	*Assets*	₹
Creditors	8,000	Machinery	30,000
Provident Fund	11,000	Furniture	32,000
Capital Accounts :		Stock	13,000
A	47,375	Debtors	15,000
B	35,625	Bank	36,000
C	24,000		
	1,26,000		1,26,000

ILLUSTRATION 52.

Murari and Vohra were partners in a firm with capitals of ₹1,20,000 and ₹1,60,000 respectively. On 1.4.2022 they admitted Yadav as a partner for one-fourth share in profits on his payment of ₹2,00,000 as his capital and ₹90,000 for his one-fourth share of goodwill.

On that date the creditors of Murari and Vohra were ₹60,000 and Bank overdraft was ₹15,000. Their assets apart from cash included Stock ₹10,000; Debtors ₹40,000; Plant and Machinery ₹80,000; Land and Building ₹2,00,000. It was agreed that stock

should be depreciated by ₹2,000; Plant and Machinery by 20%, ₹5,000 should be written off as bad debts and Land and Building should be appreciated by 25%.

Prepare Revaluation Account, Capital Accounts of Murari, Vohra and Yadav and the Balance Sheet of the new firm.

SOLUTION :

MEMORANDUM BALANCE SHEET
(Before Yadav's Admission)

Liabilities	₹	*Assets*	₹
Creditors	60,000	Stock	10,000
Bank Overdraft	15,000	Debtors	40,000
Murari's Capital A/c	1,20,000	Plant & Machinery	80,000
Vohra's Capital A/c	1,60,000	Land & Building	2,00,000
		Cash (Balancing Figure)	25,000
	3,55,000		3,55,000

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Stock		2,000	By Land & Building	50,000
To Plant & Machinery		16,000		
To Debtors		5,000		
To Profit on revaluation transferred to :				
Murari's Capital A/c	13,500			
Vohra's Capital A/c	13,500	27,000		
		50,000		50,000

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	*Murari*	*Vohra*	*Yadav*	*Particulars*	*Murari*	*Vohra*	*Yadav*
	₹	₹	₹		₹	₹	₹
To Balance c/d	1,78,500	2,18,500	2,00,000	By Balance b/d	1,20,000	1,60,000	—
				By Bank A/c	—	—	2,00,000
				By Revaluation A/c (Profit)	13,500	13,500	—
				By Premium for Goodwill A/c	45,000	45,000	—
	1,78,500	2,18,500	2,00,000		1,78,500	2,18,500	2,00,000

BALANCE SHEET OF NEW FIRM
as at 1st April, 2022

Liabilities		₹	*Assets*	₹
Creditors		60,000	Cash	25,000
Capital A/cs :			Bank Balance[(1)]	2,75,000
Murari	1,78,500		Stock	8,000

Vohra	2,18,500		Debtors	35,000
Yadav	2,00,000	5,97,000	Plant & Machinery	64,000
			Land & Building	2,50,000
		6,57,000		6,57,000

Note : (1) Bank Balance : ₹2,00,000 + ₹90,000 – Bank Overdraft ₹15,000 = ₹2,75,000

CASE BASED MCQs — 4

A, *B* and *C* are partners sharing profits in 2 : 2 : 1. *D* was admitted with 1/5th share of profits and it was agreed that *A* would retain his original share. *D* brings his share of goodwill ₹1,20,000 in Cash. Following balances appeared in their books at this date:

			₹
Plant			3,00,000
Investments			2,00,000
Investment Fluctuation Reserve			20,000
Advertisement Suspense Account			60,000
Contingency Reserve			90,000
Capitals :	*A*		4,00,000
	B		3,00,000
	C		2,00,000
Sundry Debtors		1,26,000	
Less : Provision for Doubtful Debts		8,000	1,18,000

It was agreed that :

(*i*) Plant is overvalued by 25%.

(*ii*) Market value of Investments is ₹1,50,000.

(*iii*) Bad-debts ₹6,000 be written off and provision for doubtful debts be maintained @ 10% on debtors.

You are required to choose the correct option :

(*a*) Loss on Revaluation will be :

(*i*) ₹1,20,000 (*ii*) ₹1,00,000
(*iii*) ₹1,06,000 (*iv*) ₹1,15,000

(*b*) New Profit Sharing Ratio will be :

(*i*) 2 : 2 : 1 : 1 (*ii*) 2 : 4 : 2 : 1
(*iii*) 6 : 4 : 2 : 3 (*iv*) 6 : 4 : 2 : 1

(*c*) In respect of goodwill :

(*i*) ₹1,20,000 will be credited to *A*, *B* and *C* in 2 : 2 : 1.
(*ii*) ₹1,20,000 will be credited to *B* and *C* in 2 : 1.
(*iii*) ₹ 24,000 will be credited to *B* and *C* in 2 : 1.
(*iv*) ₹1,20,000 will be credited to *A*, *B* and *C* in 6 : 4 : 2.

(*d*) *A*'s Capital A/c balance will be :

(*i*) ₹3,72,000 (*ii*) ₹3,60,000
(*iii*) ₹3,64,000 (*iv*) ₹3,69,600

(*e*) *B*'s Capital A/c balance will be :

(*i*) ₹3,40,000 (*ii*) ₹3,49,600
(*iii*) ₹3,44,000 (*iv*) ₹3,52,000

ILLUSTRATION 53.

Sunaina and Tamanna are partners in a firm sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as at 31st March, 2020 stood as follows :

BALANCE SHEET

Liabilities		₹	*Assets*		₹
Capital Accounts :			Plant & Machinery		1,20,000
Sunaina	60,000		Land and Building		1,40,000
Tamanna	80,000	1,40,000	Debtors	1,90,000	
Current Accounts :			*Less* : Provision for		
Sunaina	10,000		Doubtful Debts	(40,000)	1,50,000
Tamanna	30,000	40,000	Stock		40,000
General Reserve		1,20,000	Cash		30,000
Workmen's Compensation Reserve		50,000	Goodwill		20,000
Creditors		1,50,000			
		5,00,000			5,00,000

They agreed to admit Pranav into partnership for 1/5th share of profits on 1st April, 2020, on the following terms :

(*a*) All Debtors are good.

(*b*) Value of land and building to be increased to ₹1,80,000.

(*c*) Value of plant and machinery to be reduced by ₹20,000.

(*d*) The liability against Workmen's Compensation Reserve is determined at ₹20,000 which is to be paid later in the year.

(*e*) Mr. Anil, to whom ₹40,000 were payable (already included in above creditors), drew a bill of exchange for 3 months which was duly accepted.

(*f*) Pranav to bring in capital of ₹1,00,000 and ₹10,000 as premium for goodwill in cash.

Journalize. *(C.B.S.E. Sample Paper, 2020)*

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2020					
April 1	Land and Building A/c	Dr.		40,000	
	Provision for Doubtful Debts A/c	Dr.		40,000	
	To Revaluation A/c				80,000
	(Land and Building revalued and provision for doubtful debts written back)				

April 1	Revaluation A/c Dr.		20,000	
	To Plant and Machinery A/c			20,000
	(Plant and Machinery revalued)			
April 1	Revaluation A/c Dr.		60,000	
	To Sunaina's Current A/c			36,000
	To Tamanna's Current A/c			24,000
	(Profit on revaluation credited to partners current accounts)			
April 1	Creditors A/c Dr.		40,000	
	To Bills Payable A/c			40,000
	(Bills accepted in favour of Mr. Anil)			
April 1	Sunaina's Current A/c Dr.		12,000	
	Tamanna's Current A/c Dr.		8,000	
	To Goodwill A/c			20,000
	(Goodwill written off)			
April 1	General Reserve A/c Dr.		1,20,000	
	To Sunaina's Current A/c			72,000
	To Tamanna's Current A/c			48,000
	(Reserve distributed among old partners)			
April 1	Workmen Compensation Reserve A/c Dr.		50,000	
	To Claim for Workmen Compensation A/c			20,000
	To Sunaina's Current A/c			18,000
	To Tamanna's Current A/c			12,000
	(Provision for Workmen Compensation provided and balance distributed among old partners)			
April 1	Bank A/c Dr.		1,10,000	
	To Pranav's Capital A/c			1,00,000
	To Premium for Goodwill A/c			10,000
	(Capital and premium brought in by new partner)			
April 1	Premium for Goodwill A/c Dr.		10,000	
	To Sunaina's Current A/c			6,000
	To Tamanna's Current A/c			4,000
	(Premium distributed among sacrificing partners)			

ILLUSTRATION 54.

The following is the Balance Sheet at 31st March, 2022, of *A* and *B* who are in partnership and share profits and losses in the proportion of three-fifth and two-fifth respectively.

Liabilities	₹	*Assets*	₹
Creditors	15,000	Freehold Premises	10,000
Bills Payable	4,310	Machinery and Plant	4,500
Provision for Doubtful Debts	4,000	Furniture	900

Capital Accounts :			Stock	12,500
A	24,000		Debtors	22,500
B	9,000	33,000	Investments	4,250
			Cash	1,660
		56,310		56,310

They admit *C* into partnership from 1st April, 2022. The terms of agreement are as under :

(*i*) *C* to bring in ₹6,000 as capital and ₹4,800 for goodwill in order to get two-seventh share in profit.

(*ii*) ₹4,800 paid by *C* to be credited to the Loan Accounts of *A* and *B* in respective proportions.

(*iii*) Freehold Premises is undervalued by ₹5,000.

(*iv*) Machinery and Plant is overvalued by ₹500.

(*v*) Stock to be discounted at 10% and Provision for Doubtful Debts be reduced by ₹1,000.

(*vi*) Investments are to be brought down at their market price, it being ₹3,200.

Prepare Journal entries, capital accounts and opening balance sheet. Also calculate the new ratio.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2022					
April 1	Freehold Premises A/c	Dr.		5,000	
	Provision for Doubtful Debts A/c	Dr.		1,000	
	To Revaluation A/c				6,000
	(Increase in the value of Freehold Premises and decrease in provision for doubtful-debts.)				
	Revaluation A/c	Dr.		2,800	
	To Machinery and Plant A/c				500
	To Stock A/c				1,250
	To Investments A/c				1,050
	(Decrease in the value of Assets)				
	Revaluation A/c	Dr.		3,200	
	To *A*'s Capital A/c				1,920
	To *B*'s Capital A/c				1,280
	(Transfer of profit on revaluation)				
	Cash A/c	Dr.		10,800	
	To *C*'s Capital A/c				6,000
	To Premium for Goodwill A/c				4,800
	(Amount of capital and premium for goodwill introduced by *C*)				

Premium for Goodwill A/c	Dr.		4,800	
To *A*'s Loan A/c				2,880
To *B*'s Loan A/c				1,920
(Premium for goodwill transferred to the Loan Accounts of old partners)				

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Balance c/d	25,920	10,280	6,000	By Balance b/d	24,000	9,000	
				By Revaluation	1,920	1,280	
				By Cash			6,000
	25,920	10,280	6,000		25,920	10,280	6,000

OPENING BALANCE SHEET
as at 1st April, 2022

Liabilities	₹	*Assets*	₹
Creditors	15,000	Freehold Premises	15,000
Bills Payable	4,310	Machinery and Plant	4,000
Provision for Doubtful Debts	3,000	Furniture	900
Loan Accounts :		Stock	11,250
A	2,880	Debtors	22,500
B	1,920	Investments	3,200
Capital Accounts :		Cash	12,460
A	25,920		
B	10,280		
C	6,000		
	69,310		69,310

New Profit sharing ratios will be : C takes $\frac{2}{7}$th share out of 1.

Remaining share $= 1 - \frac{2}{7} = \frac{5}{7}$

$\therefore$ *A*'s share $= \frac{3}{5}$th of $\frac{5}{7} = \frac{3}{7}$

B's share $= \frac{2}{5}$th of $\frac{5}{7} = \frac{2}{7}$

New ratio of $A : B : C$ $= \frac{3}{7} : \frac{2}{7} : \frac{2}{7}$ or $3 : 2 : 2$.

ILLUSTRATION 55.

Quick and Slow are partners in a firm sharing profits and losses in the ratio of 3 : 2. The Balance Sheet of the firm as at 31st March, 2018 was as under :

Liabilities	₹	*Assets*	₹
Capital Accounts		Furniture & Fixtures	60,000

Quick	1,20,000		Office Equipments	30,000
Slow	77,000	1,97,000	Motor Car	75,000
General Reserve		30,000	Stock	50,000
Sundry Creditors		96,000	Sundry Debtors	90,000
			Cash at Bank	18,000
		3,23,000		3,23,000

Smooth was admitted as a new partner with effect from 1st April, 2018 and it was agreed that he would bring some private furniture worth ₹10,000 and private stock costing ₹8,000 and in addition contribute ₹50,000 cash towards capital.

He would also bring proportionate share of goodwill which is to be valued at two year's purchase of the average profits of the last three years.

The profits of the last three years were :

	₹
2017-18	52,000
2016-17	32,000
2015-16	28,000

However, on a checking of the past records, it was noticed that on 1.4.2016 some new furniture costing ₹8,000 was purchased but wrongly debited to revenue and in 2017-18 a purchase invoice for ₹4,000 dated 25.3.2018 has been omitted in the books. The firm charges depreciation on furniture @ 10% p.a. on written down value.

Your calculation of goodwill is to be made on the basis of correct profits.

On revaluation, value of stock is to be reduced by 5% and Motor car is worth ₹85,000.

Smooth duly paid the required amount for goodwill and cash towards capital.

It was decided that the future profits of the firm would be shared as Quick 50%, Slow 30% and Smooth 20%.

Assuming the above mentioned arrangements were duly carried out, show the Profit & Loss Adjustment Account, Capital Accounts of the partners and the Balance Sheet of the firm after Smooth's admission.

SOLUTION :

Ascertainment of Premium for Goodwill :

	2015-16	2016-17	2017-18
	₹	₹	₹
Profits as per P & L A/c	28,000	32,000	52,000
Purchase of Furniture on 1-4-2016			
Wrongly charged to revenue		+ 8,000	
Depreciation on Furniture :			
10% on 8,000 in 2016-17		(–) 800	
10% on 7,200 in 2017-18			(–) 720
Purchase invoice omitted from the books			(–) 4,000
Adjusted Profits	28,000	39,200	47,280

$$\text{Average Profits} = \frac{28,000 + 39,200 + 47,280}{3} = ₹38,160$$

Value of goodwill at 2 year's purchase = ₹38,160 × 2 = ₹76,320
Premium for goodwill to be brought by Smooth = 20% of ₹76,320 = ₹15,264

Ratio of Sacrifice :

$$\text{Quick} = \frac{3}{5} - \frac{5}{10} = \frac{1}{10}$$

$$\text{Slow} = \frac{2}{5} - \frac{3}{10} = \frac{1}{10}$$

∴ The Premium for Goodwill ₹15,264 contributed by Smooth will be shared equally by Quick and Slow.

Dr. PROFIT AND LOSS ADJUSTMENT ACCOUNT Cr.

Particulars		₹	Particulars	₹
To Furniture & Fixtures A/c – Depreciation (800 + 720)		1,520	By Furniture & Fixtures A/c	8,000
To Creditors A/c – purchase invoice omitted		4,000	By Motor Car A/c	10,000
To Stock A/c		2,500		
To Profit on adjustment and revaluation :				
Quick's Capital A/c	5,988			
Slow's Capital A/c	3,992	9,980		
		18,000		18,000

Journal Entry for the Capital Contributed by Smooth

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2018					
April 1	Furniture A/c	Dr.		10,000	
	Stock A/c	Dr.		8,000	
	Cash A/c	Dr.		50,000	
	To Smooth's Capital A/c				68,000
	(Assets brought in by Smooth towards his capital)				

Dr. CAPITAL ACCOUNTS Cr.

Particulars	Quick	Slow	Smooth	Particulars	Quick	Slow	Smooth
1.4.2018	₹	₹	₹	31.3.2018	₹	₹	₹
To Balance c/d	1,51,620	1,00,624	68,000	By Balance b/d	1,20,000	77,000	—
				1.4.2018			
				By General Reserve A/c	18,000	12,000	—
				By Sundry Assets A/c			68,000

				By Premium for Goodwill A/c	7,632	7,632	
				By P & L Adj. A/c	5,988	3,992	—
	1,51,620	1,00,624	68,000		1,51,620	1,00,624	68,000

BALANCE SHEET
as at 1st April, 2018

Liabilities		₹	*Assets*	₹
Capital Accounts :			Furniture & Fixtures (60,000 + 10,000 + 8,000 – 1,520)	76,480
Quick	1,51,620		Office Equipments	30,000
Slow	1,00,624		Motor Car	85,000
Smooth	68,000	3,20,244	Stock (50,000 + 8,000 – 2,500)	55,500
Sundry Creditors (96,000 + 4,000)		1,00,000	Sundry Debtors	90,000
			Cash at Bank (18,000 + 50,000 + 15,264)	83,264
		4,20,244		4,20,244

ILLUSTRATION 56.

X and *Y* are in partnership sharing profits and losses in the ratio of 2 : 1. As from 1st April, 2022 they admit *Z* into partnership and the new ratio of *X, Y* and *Z* is agreed as $\frac{1}{4} : \frac{3}{8} : \frac{3}{8}$. *Z* is to contribute a sum of ₹1,50,000 as his capital and ₹36,000 as his share of goodwill. The Balance Sheet of *X* and *Y* as at 31st March, 2022 stood as follows :

Liabilities	₹	*Assets*	₹
Creditors	70,000	Land & Buildings	3,40,000
Capital Accounts :		Plant	2,00,000
X	4,00,000	Stock	80,000
Y	2,50,000	Debtors	75,000
		Cash and Bank	25,000
	7,20,000		7,20,000

Land & Buildings are to be valued at ₹3,00,000. Plant is to be depreciated by 10% and stock by ₹6,000.

Give journal entries to record the above transactions and prepare the opening balance sheet of the new firm. Revaluation is to be made through Profit & Loss Adjustment A/c.

SOLUTION :

Old Ratio of *X* and *Y* = 2 : 1

New Ratio of *X, Y* and *Z* = $\frac{1}{4} : \frac{3}{8} : \frac{3}{8}$

Sacrifice or Gain :

$$X = \frac{2}{3} - \frac{1}{4} = \frac{16-6}{24} = \frac{10}{24} \text{ (Sacrifice)}$$

$$Y = \frac{1}{3} - \frac{3}{8} = \frac{8-9}{24} = \frac{1}{24} \text{ (Gain)}$$

$$Z = \frac{3}{8} \text{ or } \frac{9}{24} \text{ (Gain)}$$

Only *X* is sacrificing his share to the benefit of *Y* and *Z*. Hence, the whole amount of premium brought in by *Z* will be credited to *X*. In addition, *Y* must also compensate *X* for acquiring $\frac{1}{24}$ share. The value of whole of firm's goodwill on the basis of premium paid by *Z* is ₹36,000 $\times \frac{8}{3}$ = ₹96,000. On this basis the amount of compensation to be paid by *Y* will be ₹96,000 $\times \frac{1}{24}$ = ₹4,000.

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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022 April 1	Profit & Loss Adjustment A/c	Dr.		66,000	
	To Land and Buildings A/c				40,000
	To Plant A/c				20,000
	To Stock A/c				6,000
	(Decrease in the value of assets)				
	X's Capital A/c	Dr.		44,000	
	Y's Capital A/c	Dr.		22,000	
	To Profit & Loss Adjustment A/c				66,000
	(Transfer of loss on revaluation in the ratio of 2 : 1)				
	Bank A/c	Dr.		1,86,000	
	To Z's Capital A/c				1,50,000
	To Premium for Goodwill A/c				36,000
	(Amount introduced by Z for capital and premium for goodwill)				
	Premium for Goodwill A/c	Dr.		36,000	
	To X's Capital A/c				36,000
	(Premium for goodwill brought in by Z credited to sacrificing partner X)				
	Y's Capital A/c	Dr.		4,000	
	To X's Capital A/c				4,000
	(Adjustment for goodwill on acquiring 1/24 share by Y from X)				

Dr. CAPITAL ACCOUNTS Cr.

Particulars	X	Y	Z	Particulars	X	Y	Z
	₹	₹	₹		₹	₹	₹
To Profit & Loss Adj. A/c	44,000	22,000		By Balance b/d	4,00,000	2,50,000	
				By Bank			1,50,000

Particulars	X	Y	Z	Particulars	X	Y	Z
To X's Capital A/c		4,000		By Premium for Goodwill A/c	36,000		
To Balance c/d	3,96,000	2,24,000	1,50,000	By Y's Capital A/c	4,000		
	4,40,000	2,50,000	1,50,000		4,40,000	2,50,000	1,50,000

BALANCE SHEET

as at 1st April, 2022

Liabilities	₹	*Assets*	₹
Creditors	70,000	Land and Buildings	3,00,000
Capital Accounts :		Plant	1,80,000
X	3,96,000	Stock	74,000
Y	2,24,000	Debtors	75,000
Z	1,50,000	Cash and Bank	2,11,000
	8,40,000		8,40,000

ILLUSTRATION 57.

Following is the Balance Sheet of *A*, *B* and *C* who share profits and losses of the business in the ratio of 3 : 2 : 1.

BALANCE SHEET

as at 31st March, 2022

Liabilities		₹	*Assets*	₹
Capital A/cs :			Furniture	95,000
A	1,20,000		Business Premises	2,05,000
B	1,20,000		Stock-in-Trade	40,000
C	1,20,000	3,60,000	Debtors	28,000
Sundry Creditors		20,000	Cash at Bank	15,000
Outstanding Salaries and Wages		7,200	Cash in Hand	4,200
		3,87,200		3,87,200

On 1st April, 2022, they admit *D* as a partner on the following conditions :

(*i*) *D* will bring ₹1,20,000 as his Capital and also ₹30,000 as Goodwill premium for a quarter of the share in the future profit/loss of the firm.

(*ii*) The values of the fixed assets of the firm will be increased by 10% before the admission of *D*.

(*iii*) The future profits and losses of the firm will be shared equally by the partners.

Show Journal entries, Revaluation Account, Partner's Capital Accounts and the opening Balance Sheet of the new firm to include the above-mentioned transactions assuming that the conditions were duly satisfied.

SOLUTION:

Books of *A*, *B*, *C* and *D*

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
April 1	Furniture A/c	Dr.		9,500	
	Business Premises A/c	Dr.		20,500	
	To Revaluation A/c				30,000
	(Increase in the value of assets)				
	Revaluation A/c	Dr.		30,000	
	To *A*'s Capital A/c				15,000
	To *B*'s Capital A/c				10,000
	To *C*'s Capital A/c				5,000
	(Transfer of profit on revaluation in the ratio of 3 : 2 : 1)				
	Bank A/c	Dr.		1,50,000	
	To *D*'s Capital A/c				1,20,000
	To Premium for Goodwill A/c				30,000
	(Amount brought in by *D* for capital and premium for goodwill)				
	Premium for Goodwill A/c	Dr.		30,000	
	To *A*'s Capital A/c				22,500
	To *B*'s Capital A/c				7,500
	(Premium for goodwill brought in by *D* credited to *A* and *B* in their sacrificing ratio of 3 : 1)				
	C's Capital A/c	Dr.		10,000	
	To *A*'s Capital A/c				7,500
	To *B*'s Capital A/c				2,500
	(Adjustment for goodwill for acquiring $\frac{1}{12}$th share by *C* from *A* and *B* in their sacrificing ratio of 3 : 1)				

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	Particulars	₹
To Profit on revaluation transferred to :			By Furniture A/c	9,500
A's Capital A/c	15,000		By Business Premises A/c	20,500
B's Capital A/c	10,000			
C's Capital A/c	5,000	30,000		
		30,000		30,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*D*	Particulars	*A*	*B*	*C*	*D*
	₹	₹	₹	₹		₹	₹	₹	₹
To *A*'s Capital A/c	—	—	7,500	—	By Bal. b/d	1,20,000	1,20,000	1,20,000	—
					By				

To *B*'s Capital A/c	—	—	2,500	—	By Revaluation A/c (profit)	15,000	10,000	5,000	—
To Bal. c/d	1,65,000	1,40,000	1,15,000	1,20,000	By Bank A/c	—	—	—	1,20,000
					By Premium for goodwill A/c	22,500	7,500	—	—
					By *C*'s Capital A/c	7,500	2,500	—	—
	1,65,000	1,40,000	1,25,000	1,20,000		1,65,000	1,40,000	1,25,000	1,20,000

BALANCE SHEET
as at 1st April, 2022

Liabilities		₹	*Assets*	₹
Capital Accounts :			Business Premises	2,25,500
A	1,65,000		Furniture	1,04,500
B	1,40,000		Stock-in-Trade	40,000
C	1,15,000		Debtors	28,000
D	1,20,000	5,40,000	Cash at Bank	1,65,000
Sundry Creditors		20,000	Cash in Hand	4,200
Outstanding Salaries and Wages		7,200		
		5,67,200		5,67,200

Working Notes :

(*i*) Old Ratio of *A*, *B* and *C* $= 3 : 2 : 1$

New Ratio of *A*, *B*, *C* and *D* $= \frac{1}{4} : \frac{1}{4} : \frac{1}{4} : \frac{1}{4}$

Sacrifice or Gain :

$$A = \frac{3}{6} - \frac{1}{4} = \frac{6-3}{12} = \frac{3}{12} \quad \text{(Sacrifice)}$$

$$B = \frac{2}{6} - \frac{1}{4} = \frac{4-3}{12} = \frac{1}{12} \quad \text{(Sacrifice)}$$

$$C = \frac{1}{6} - \frac{1}{4} = \frac{2-3}{12} = \frac{1}{12} \quad \text{(Gain)}$$

(*ii*) Entire amount of premium for goodwill paid by *D* will be credited to *A* and *B* in their sacrificing ratio of 3 : 1.

(*iii*) In addition, *C* will compensate *A* and *B* for acquiring $\frac{1}{12}$th share on the basis of premium paid by *D*. The amount of compensation will be :

Value of whole of firm's goodwill $= ₹30,000 \times \frac{4}{1} = ₹1,20,000$

Compensation paid by *C* $= ₹1,20,000 \times \frac{1}{12} = ₹10,000$

ILLUSTRATION 58.

A, *B* and *C* were in partnership sharing profit in the proportions of 3 : 2 : 1. Their Balance Sheet as at 31st Jan., 2022 was as under :

Liabilities		₹	*Assets*	₹
Sundry Creditors		72,100	Goodwill	12,000
Capital Accounts :			Sundry Assets	7,18,000
A	3,00,000			
B	2,20,000			
C	1,20,000	6,40,000		
Current Accounts :				
A	12,000			
B	3,500			
C	2,400	17,900		
		7,30,000		7,30,000

On 1st February, 2022, *D* was introduced as a partner, bringing in ₹1,25,000 in cash as his capital and a further ₹30,000 for his share of goodwill. He was to take 1/6th share of profits, the old partners sharing the balance in the proportions of 8 : 4 : 3.

Make the necessary journal entries to record the above transactions and prepare the opening Balance Sheet of the new firm.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
Feb. 1	*A*'s Current A/c	Dr.		6,000	
	B's Current A/c	Dr.		4,000	
	C's Current A/c	Dr.		2,000	
	To Goodwill A/c				12,000
	(Goodwill written off in old profit sharing ratio *i.e.* 3 : 2 : 1)				
	Bank A/c	Dr.		1,55,000	
	To *D*'s Capital A/c				1,25,000
	To Premium for Goodwill A/c				30,000
	(Amount of Capital and premium for goodwill introduced by *D*)				

	Premium for Goodwill A/c Dr.		30,000	
	To *A*'s Current A/c			10,000
	To *B*'s Current A/c			20,000
	(Premium for goodwill transferred to *A* and *B* in their sacrificing ratio *i.e.*, 1 : 2)			

Dr. PARTNER'S CURRENT ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Goodwill A/c	6,000	4,000	2,000	By Bal. b/d	12,000	3,500	2,400
To Bal. c/d	16,000	19,500	400	By Premium for Goodwill A/c	10,000	20,000	
	22,000	23,500	2,400		22,000	23,500	2,400

BALANCE SHEET

as at 1st Feb., 2022

Liabilities	₹	*Assets*	₹
Sundry Creditors	72,100	Sundry Assets	7,18,000
Capital Accounts :		Bank	1,55,000
A	3,00,000		
B	2,20,000		
C	1,20,000		
D	1,25,000		
Current Accounts :			
A	16,000		
B	19,500		
C	400		
	8,73,000		8,73,000

Working Notes :

1. *D* is admitted for 1/6th share. Balance 5/6th will be shared by other partners in their revised ratio of 8 : 4 : 3. Hence, new ratio is :

$$A = \frac{8}{15} \times \frac{5}{6} = \frac{8}{18}$$

$$B = \frac{4}{15} \times \frac{5}{6} = \frac{4}{18}$$

$$C = \frac{3}{15} \times \frac{5}{6} = \frac{3}{18}$$

$$D = \frac{1}{6} = \frac{3}{18}$$

Sacrificing Ratio =

$$A = \frac{3}{6} - \frac{8}{18} = \frac{1}{18}$$

$$B = \frac{2}{6} - \frac{4}{18} = \frac{2}{18}$$

$$C = \frac{1}{6} - \frac{3}{18} = 0$$

Hence, *A* and *B* sacrifice in the ratio of 1 : 2 and *C* makes no sacrifice.

When new partner does not bring his share of goodwill in cash :

ILLUSTRATION 59 (A).

A and *B* are partners in a firm. Their balance sheet as at 31st March, 2019 was as follows :

Liabilities	₹	*Assets*	₹
Provision for Doubtful Debts	4,000	Cash	10,000
Workmen Compensation Reserve	5,600	Sundry Debtors	80,000
Outstanding Expenses	3,000	Stock	20,000
Creditors	30,000	Fixed Assets	38,600
Capitals : *A*	50,000	Profit & Loss A/c	4,000
B	60,000		
	1,52,600		1,52,600

C was taken into partnership as from 1st April, 2019. *C* brought ₹40,000 as his capital but he is unable to bring any amount for goodwill. New profit sharing ratio is 3 : 2 : 1. Following terms were agreed upon :

1. Claim on account of Workmen's Compensation is ₹3,000.
2. To write off Bad Debts amounting to ₹6,000.
3. Creditors are to be paid ₹2,000 more.
4. ₹2,000 be provided for an unforeseen liability.
5. Outstanding expenses be brought down to ₹1,200.
6. Goodwill is valued at $1\frac{1}{2}$ years' purchase of the average profits of last three years. Profits of 3 years amounted to ₹8,000; ₹10,000 and ₹18,000.

Prepare Journal entries, capital accounts and opening Balance Sheet.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2019					
April 1	*A*'s Capital A/c	Dr.		2,000	
	B's Capital A/c	Dr.		2,000	
	To Profit & Loss A/c				4,000
	(Loss appearing in the Balance Sheet debited to old partner's accounts)				
	Workmen Compensation Reserve A/c[(1)]	Dr.		5,600	
	To Liability for Workmen Compensation Claim A/c				3,000
	To *A*'s Capital A/c				1,300
	To *B*'s Capital A/c				1,300
	(Excess Reserve (₹5,600 – 3,000) shared by old partners)				

Bad Debts A/c To Sundry Debtors (Bad Debt written off)	Dr.		6,000	6,000
Provision for Doubtful Debts A/c(2) Revaluation A/c To Bad Debt A/c (Bad Debts adjusted)	Dr. Dr.		4,000 2,000	6,000
Revaluation A/c To Creditors A/c To Unforeseen Liability A/c (Provision for Liabilities)	Dr.		4,000	2,000 2,000
Outstanding Expenses A/c To Revaluation A/c (Outstanding expenses reduced)	Dr.		1,800	1,800
A's Capital A/c *B*'s Capital A/c To Revaluation A/c (Loss on revaluation transferred)	Dr. Dr.		2,100 2,100	4,200
C's Current A/c(4) To *B*'s Capital A/c (*C*'s share of goodwill credited to *B*'s Capital A/c, as he alone has sacrificed)	Dr.		3,000	3,000
Cash A/c To *C*'s Capital A/c (Cash brought in by *C* as capital)	Dr.		40,000	40,000

Note : Students are advised to prepare Revaluation a/c themselves.

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To P & L A/c	2,000	2,000		By Bal. b/d	50,000	60,000	
To Revaluation	2,100	2,100		By Workmen's compensation fund	1,300	1,300	
To Bal. c/d	47,200	60,200	40,000	By *C*'s Current A/c		3,000	
				By Cash			40,000
	51,300	64,300	40,000		51,300	64,300	40,000

OPENING BALANCE SHEET *as at 1st April, 2019*

Liabilities	₹	*Assets*	₹
Liability for Workmen Compensation Claim	3,000	Cash	50,000
Outstanding Expenses	1,200	Sundry Debtors	74,000
Unforeseen Liability	2,000	Stock	20,000
		Fixed Assets	38,600

Creditors		32,000	C's Current A/c	3,000
Capitals	*A*	47,200		
	B	60,200		
	C	40,000		
		1,85,600		1,85,600

Notes: 1. Workmen Compensation Reserve is appearing at ₹5,600, whereas, the actual liability for Workmen's Compensation is ₹3,000. Therefore, ₹2,600 will be transferred to the capital accounts of old partners in their old ratio.

2. Provision for Doubtful debts appearing in the balance sheet is ₹4,000, whereas actual bad debts amounted to ₹6,000. Therefore, ₹2,000 will be debited to revaluation account as loss.

3. Valuation of Goodwill

$$\text{Average Profit} = \frac{8,000 + 10,000 + 18,000}{3} = ₹12,000$$

$$12,000 \times 1\frac{1}{2} = ₹18,000$$

$$\text{C's share of Goodwill} = 18,000 \times \frac{1}{6} = ₹3,000.$$

Sacrifice Ratio = (Old Ratio – New Ratio)

$$A = \frac{1}{2} - \frac{3}{6} = 0$$

$$B = \frac{1}{2} - \frac{2}{6} = \frac{1}{6}$$

Hence, *B* alone has sacrificed.

4. From C's share of goodwill, his Current A/c has been debited instead of his Capital A/c so that his Capital is not reduced and remains intact at ₹40,000.

ILLUSTRATION 59 (B).

X and *Y* are in partnership, sharing profits in the ratio of 5 : 3 respectively. Their balance sheet is as follows :

Liabilities		₹	*Assets*		₹
Creditors		28,000	Cash at Bank		15,800
Workmen's Compensation			Debtors	40,000	
Reserve		12,000	*Less* : Provision	1,800	38,200
Z's Loan A/c		30,000	Stock		56,000
Capital A/cs :			Investments		10,000
	X	50,000	Goodwill		10,000
	Y	40,000	Plant		30,000
		1,60,000			1,60,000

Z is admitted into partnership on the following terms :

(1) The new profit-sharing ratio will be 4 : 3 : 2 between *X, Y* and *Z* respectively.

(2) *Z*'s loan should be treated as his capital.

(3) Goodwill of the firm is valued at ₹27,000.

(4) ₹8,000 of investments were to be taken over by *X* and *Y* in their profit sharing ratio.

(5) Stock be reduced by 10%.

(6) Provision for doubtful debts should be @ 5% on debtors and a provision for discount on debtors @ 2% should also be made.

(7) The liability of Workmen's Compensation Reserve was determined to be ₹15,000.

(8) *X* is to withdraw ₹6,000 in cash.

Give journal entries to record the above and prepare balance sheet of the new firm.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Revalutation A/c	Dr.		6,560	
	To Stock A/c				5,600
	To Provision for Doubtful Debts				200
	To Provision for Discount on Debtors				760
	(Decrease in the value of stock and creation of provision on debtors)				
	Workmen's Compensation Reserve A/c	Dr.		12,000	
	Revaluation A/c	Dr.		3,000	
	To Liability for Workmen's Compensation A/c				15,000
	(Recording of liability for Workmen's Compensation)				
	X's Capital A/c	Dr.		5,975	
	Y's Capital A/c	Dr.		3,585	
	To Revaluation A/c				9,560
	(Loss on revaluation transferred to old partners' Capital A/cs)				
	X's Capital A/c	Dr.		5,000	
	Y's Capital A/c	Dr.		3,000	
	To Investments A/c				8,000
	(Investments taken over by old partners)				
	X's Capital A/c	Dr.		6,250	
	Y's Capital A/c	Dr.		3,750	
	To Goodwill A/c				10,000
	(Existing goodwill written off in old ratio *i.e.*, 5 : 3)				
	Z's Current A/c(2)	Dr.		6,000	
	To *X*'s Capital A/c				4,875
	To *Y*'s Capital A/c				1,125
	(*Z*'s share of goodwill credited to old partners in the sacrificing ratio *i.e.*, 13 : 3)				
	Z's Loan A/c	Dr.		30,000	
	To *Z*'s Capital A/c				30,000
	(*Z*'s Loan Account transferred to *Z*'s Capital Account)				
	X's Capital A/c	Dr.		6,000	
	To Bank A/c				6,000
	(Cash withdrew by *X*)				

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	*X*	*Y*	*Z*	*Particulars*	*X*	*Y*	*Z*
	₹	₹	₹		₹	₹	₹
To Revaluation	5,975	3,585	—	By Balance b/d	50,000	40,000	—
To Investments	5,000	3,000	—	By Z's Current A/c	4,875	1,125	—
To Goodwill A/c	6,250	3,750	—	By Z's Loan A/c	—	—	30,000
To Bank A/c	6,000	—	—				
To Balance c/d	31,650	30,790	30,000				
	54,875	41,125	30,000		54,875	41,125	30,000

BALANCE SHEET

as at ....

Liabilities		₹	*Assets*		₹
Creditors		28,000	Cash at Bank (₹15,800 – ₹6,000)		9,800
Liability for Workmen's Compensation		15,000	Debtors	40,000	
Capital A/cs :			*Less :* Provision for Doubtful Debts	2,000	
X	31,650			38,000	
Y	30,790				
Z	30,000	92,440	*Less :* Provision for Discount on Debtors	760	37,240
			Stock		50,400
			Investments		2,000
			Plant		30,000
			Z's Current A/c		6,000
		1,35,440			1,35,440

Note 1 : Calculation of sacrificing ratio :

Sacrificing ratio = Old ratio – New ratio

$$X = \frac{5}{8} - \frac{4}{9} = \frac{45-32}{72} = \frac{13}{72}$$

$$Y = \frac{3}{8} - \frac{3}{9} = \frac{27-24}{72} = \frac{3}{72}$$

Sacrificing Ratio = 13 : 3

Note 2 : From Z's share of goodwill, his Current A/c has been debited instead of his Capital A/c so that his Capital is not reduced and remains intact at ₹30,000.

CASE BASED MCQs — 5

A, B and *C* are partners sharing profits in 3 : 2 : 1. They admitted *D* as a new partner. On this date following balances have been extracted from their books :

	₹
A's Capital	5,00,000
B's Capital	3,00,000
C's Capital	2,00,000
Building	6,00,000

Workmen Compensation Reserve	70,000
Bills Receivables	50,000

D was given 1/6th share of profits which he acquires from *A* and *B* in the ratio of 2 : 1. It was further agreed that :

(*i*) Goodwill of the firm is valued at ₹3,60,000. *D* brings half of his share of goodwill in Cash.

(*ii*) Building is undervalued by 20%.

(*iii*) There is an unrecorded asset of ₹60,000.

(*iv*) Liability for Workmen Compensation claim is estimated at ₹1,00,000.

(*v*) A bill of exchange of ₹20,000 which was previously discounted with the bank had dishonoured but no entry has been passed for dishonour.

Based on the above information you are required to answer the following questions :

(*a*) Gain on revaluation will be

(*i*) ₹1,50,000 (*ii*) ₹1,60,000
(*iii*) ₹1,80,000 (*iv*) ₹2,10,000

(*b*) New Profit Sharing Ratio will be :

(*i*) 3 : 2 : 1 : 1 (*ii*) 7 : 5 : 2 : 2
(*iii*) 7 : 5 : 1 : 1 (*iv*) 7 : 5 : 3 : 3

(*c*)

(*i*)	Premium for Goodwill A/c	Dr.		60,000	
	To *A*'s Capital A/c				40,000
	To *B*'s Capital A/c				20,000
(*ii*)	*D*'s Current A/c	Dr.		60,000	
	To *A*'s Capital A/c				40,000
	To *B*'s Capital A/c				20,000
(*iii*)	Premium for Goodwill A/c	Dr.		30,000	
	D's Current A/c	Dr.		30,000	
	To *A*'s Capital A/c				40,000
	To *B*'s Capital A/c				20,000
(*iv*)	Premium for Goodwill A/c	Dr.		30,000	
	D's Current A/c	Dr.		30,000	
	To *A*'s Current A/c				40,000
	To *B*'s Current A/c				20,000

(*d*) Entry for dishonour of Bill of Exchange will be :

(*i*) Dr. Revaluation A/c; Cr. B/R A/c
(*ii*) Dr. Revaluation A/c; Cr. Bank A/c
(*iii*) Dr. Debtors A/c; Cr. Bank A/c
(*iv*) Dr. Debtors A/c; Cr. B/R A/c

(*e*) *A*'s Capital A/c balance will be :

(*i*) ₹6,30,000 (*ii*) ₹6,15,000
(*iii*) ₹6,45,000 (*iv*) ₹6,20,000

ILLUSTRATION 60.

X, Y, Z are partners sharing profits and losses in the ratio of 2 : 2 : 1 respectively. Their Balance Sheet as at 31st March 2003 is as given below :

BALANCE SHEET *as at 31st March 2003*

Liabilities	₹	*Assets*	₹
Sundry Creditors	51,400	Land and Building	1,00,000
O/s Liabilities	6,000	Furniture	26,000
General Reserve	26,000	Stock	47,000
Capital :		Sundry Debtors	22,000
X	48,000	Cash	4,400
Y	48,000		
Z	20,000		
	1,99,400		1,99,400

The partners decided to admit Mr. *T* as a partner with effect from 1st April 2003, on the following terms :

(*i*) Mr. *T* will bring ₹20,000 as capital and ₹10,000 as his share of goodwill.

(*ii*) Mr. *T* could bring only ₹2,500 as goodwill in cash.

(*iii*) The value of stock should be increased by ₹10,000. The furniture should be depreciated by 10% and value of land and building should be enhanced by 20%.

(*iv*) Provision for bad and doubtful debts should be made at 10% of the debtors.

(*v*) The outstanding liability includes ₹2,000 due to Mr. *R* which has been paid by Mr. *X* privately. Necessary entry is to be passed to reimburse Mr. *X* before admitting the new partner.

(*vi*) The new profit sharing ratio for *X, Y, Z, T* is 5 : 5 : 3 : 2.

(*vii*) Creditors include ₹5,000 received as commission from Mr. *A*.

Give necessary journal entries to incorporate the above changes. Also prepare capital accounts of partners and balance sheet of the new firm. *(I.S.C. 2004)*

SOLUTION :

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Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2003					
April 1	General Reserve A/c	Dr.		26,000	
	To *X*'s Capital A/c				10,400
	To *Y*'s Capital A/c				10,400
	To *Z*'s Capital A/c				5,200
	(General Reserve credited to old partners)				

Stock A/c	Dr.	10,000	
Land and Building A/c	Dr.	20,000	
To Revaluation A/c			30,000
(Increase in the value of assets)			
Revaluation A/c	Dr.	4,800	
To Furniture A/c			2,600
To Provision for Doubtful Debts A/c			2,200
(Decrease in the value of furniture and creation of provision on debtors)			
Sundry Creditors A/c	Dr.	5,000	
To Revaluation A/c			5,000
(Commission received from *A* wrongly included in Sundry Creditors)			
Revaluation A/c	Dr.	30,200	
To *X*'s Capital A/c			12,080
To *Y*'s Capital A/c			12,080
To *Z*'s Capital A/c			6,040
(Profit on revaluation transferred to old partners)			
Outstanding Liabilities A/c	Dr.	2,000	
To *X*'s Capital A/c			2,000
(Outstanding liability paid by *X* brought into account)			
Cash A/c	Dr.	22,500	
To *T*'s Capital A/c			20,000
To Premium for Goodwill A/c			2,500
(Amount brought in by *T* as his capital and a part of his share of goodwill)			
Premium for Goodwill A/c	Dr.	2,500	
T's Current A/c	Dr.	7,500	
To *X*'s Capital A/c			5,000
To *Y*'s Capital A/c			5,000
(Goodwill/premium credited to old partners in their sacrificing ratio, *i.e.* 1 : 1)			

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*X*	*Y*	*Z*	*T*	*Particulars*	*X*	*Y*	*Z*	*T*
	₹	₹	₹	₹		₹	₹	₹	₹
To Bal. C/d	77,480	75,480	31,240	20,000	By Bal. b/d	48,000	48,000	20,000	—
					By Gen. Res.	10,400	10,400	5,200	—
					By Rev.	12,080	12,080	6,040	—
					By Outstanding Liability	2,000	—	—	—
					By Cash	—	—	—	20,000
					By Sundries				

					(Premium for Goodwill)	5,000	5,000	—	—
	77,480	75,480	31,240	20,000		77,480	75,480	31,240	20,000

BALANCE SHEET

as at 1st April, 2003

Liabilities	₹	*Assets*		₹
Sundry Creditors	46,400	Land and Building		1,20,000
Outstanding Liabilities	4,000	Furniture		23,400
Capital Accounts :		Stock		57,000
X	77,480	Sundry Debtors	22,000	
Y	75,480	*Less* : Provision for		
Z	31,240	Doubtful Debts	2,200	19,800
T	20,000	Cash		26,900
		T's Current A/c		7,500
	2,54,600			2,54,600

Working Notes : (1) Sacrificing Ratio = Old Ratio – New Ratio

$$X = \frac{2}{5} - \frac{5}{15} = \frac{1}{15}$$

$$Y = \frac{2}{5} - \frac{5}{15} = \frac{1}{15}$$

$$Z = \frac{1}{5} - \frac{3}{15} = \frac{1}{15} = 0$$

Only *X* and *Y* have sacrificed in the ratio of 1 : 1.

(2) *T*'s Current A/c has been debited instead of his Capital A/c.

ILLUSTRATION 61.

X and *Y* were partners in a firm sharing profits and losses in the ratio of 7 : 3. On 31st March, 2022, their Balance Sheet was as under :

Liabilities		₹	*Assets*		₹
Creditors		3,10,000	Bank		50,000
Contingency Reserve		50,000	Debtors	4,20,000	
Capital A/cs :			*Less :* Provision for		
X	6,00,000		Doubtful Debts	20,000	4,00,000
Y	4,00,000	10,00,000	Stock		7,20,000
			Furniture		1,10,000
			Goodwill		80,000
		13,60,000			13,60,000

On the above date *Z* is admitted as a partner. *X* surrendered 1/7th of his share and *Y* 1/3rd of his share in favour of *Z*. Goodwill is valued at ₹3,00,000. *Z* brings in only 1/3rd of his share of goodwill in cash and ₹5,00,000 as his capital. Following adjustments are agreed upon :

(i) Stock is to be reduced to ₹6,00,000 and furniture by ₹30,000.

(ii) Liability for Workmen's Compensation claim to the extent of ₹18,000 would be created.

(iii) All Debtors are good.

(iv) There is an outstanding claim for damages of ₹50,000 and it is to be provided in the books.

(v) Creditors will be written back by ₹40,000.

(vi) Insurance premium amounting to ₹20,000 was debited to P & L A/c, of which ₹8,000 is related to the period after 31st March, 2022.

You are required to prepare Revaluation Account, Partner's Capital Accounts and the Balance Sheet of the new firm. Also calculate the new profit sharing ratio.

SOLUTION:

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Stock	1,20,000	By Provision for Doubtful Debts		20,000
To Furniture	30,000	By Creditors		40,000
To Workmen's Compensation Claim	18,000	By Prepaid Insurance		8,000
To Damages Payable	50,000	By Loss transferred to :		
		X's Capital A/c	1,05,000	
		Y's Capital A/c	45,000	1,50,000
	2,18,000			2,18,000

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	X	Y	Z	*Particulars*	X	Y	Z
	₹	₹	₹		₹	₹	₹
To Revaluation A/c	1,05,000	45,000		By Balance b/d	6,00,000	4,00,000	
To Goodwill A/c (Written off in 7 : 3)	56,000	24,000		By Contingency Reserve	35,000	15,000	
To Balance c/d	5,04,000	3,76,000	5,00,000	By Premium for Goodwill (1 : 1)	10,000	10,000	
				By Z's Current A/c (1 : 1)	20,000	20,000	
				By Bank			5,00,000
	6,65,000	4,45,000	5,00,000		6,65,000	4,45,000	5,00,000

BALANCE SHEET
as at 1st April, 2022

Liabilities	₹	*Assets*	₹
Creditors	2,70,000	Bank	5,70,000
Liability for Workmen's Compensation Claim	18,000	Debtors	4,20,000
		Stock	6,00,000

Outstanding claim for Damages		50,000	Furniture		80,000
Capital Accounts :			Prepaid Insurance		8,000
X	5,04,000		*Z*'s Current A/c		40,000
Y	3,76,000				
Z	5,00,000	13,80,000			
		17,18,000			17,18,000

Working Notes :

(*i*) **Calculation of Sacrificing Ratios :**

X's old share $= \frac{7}{10}$; *X* surrenders $\frac{1}{7}$th of $\frac{7}{10}$ in favour of *Z*.

It means *X* has surrendered $\frac{1}{7} \times \frac{7}{10} = \frac{1}{10}$

Y's old share $= \frac{3}{10}$; *Y* surrenders $\frac{1}{3}$rd of $\frac{3}{10}$ in favour of *Z*;

It means *Y* has surrendered $\frac{1}{3} \times \frac{3}{10} = \frac{1}{10}$

$\therefore$ Sacrificing Ratio $= X\frac{1}{10} : Y\frac{1}{10} = 1 : 1$

(*ii*) **Calculation of New Ratios :**

X's new share $= \frac{7}{10} - \frac{1}{10} = \frac{6}{10}$

Y's new share $= \frac{3}{10} - \frac{1}{10} = \frac{2}{10}$

Z's share $= \frac{1}{10} + \frac{1}{10} = \frac{2}{10}$

Hence, the new ratios of *X*, *Y* and *Z* $= \frac{6}{10} : \frac{2}{10} : \frac{2}{10} = 3 : 1 : 1$

(*iii*) *Z*'s share of Goodwill $= 3{,}00{,}000 \times \frac{1}{5} = 60{,}000$.

Out of this, $\frac{1}{3}$ *i.e.* ₹20,000 is brought in Cash and the remaining ₹40,000 is not brought in cash.

Entry for Goodwill :

Z's Current A/c	Dr.	40,000	
To *X*'s Capital A/c			20,000
To *Y*'s Capital A/c			20,000

CASE BASED MCQs — 6

A, *B* and *C* are partners sharing profits in 3 : 2 : 1. They admit *D* as a new partner for 1/4th share in the profits and he brought in ₹3,00,000 as his share of goodwill which was credited to the Capital Accounts of *B* and *C* respectively with ₹2,50,000 and ₹50,000.

Their Balance Sheet as at date was as under :

Liabilities	₹	Assets		₹
A's Capital	4,00,000	Goodwill		1,20,000
B's Capital	2,00,000	Land and Building		5,00,000
C's Capital	2,00,000	Machinery		1,00,000
Creditors	1,50,000	Furniture		40,000
General Reserve	30,000	Debtors	2,00,000	
		Less : Provision for Doubtful Debts	8,000	1,92,000
		Cash at Bank		28,000
	9,80,000			9,80,000

Following adjustments are agreed upon :

(*i*) Machinery is reduced by ₹60,000.

(*ii*) Furniture is reduced to ₹15,000.

(*iii*) An unrecorded accrued income of ₹10,600 is to be accounted.

(*iv*) A debtor whose dues of ₹50,000 were written off as bad debts, paid ₹30,000 in full settlement.

(*v*) Bad debts amounting to ₹10,000 are to be written off and provision for doubtful debts is to be maintained at the existing rate.

Based on above information, you are required to answer the following :

(*a*) Loss on revaluation will be :

(*i*) ₹56,000 (*ii*) ₹24,000
(*iii*) ₹84,000 (*iv*) ₹54,000

(*b*) New Profit Sharing Ratio will be :

(*i*) 3 : 2 : 1 : 1 (*ii*) 9 : 6 : 3 : 4
(*iii*) 4 : 1 : 1 : 2 (*iv*) 3 : 5 : 1 : 1

(*c*) *A*'s Capital Account Balance will be :

(*i*) ₹3,13,000 (*ii*) ₹3,28,000
(*iii*) ₹3,43,000 (*iv*) ₹3,88,000

(*d*) *C*'s Capital Account Balance will be :

(*i*) ₹2,26,000 (*ii*) ₹2,21,000
(*iii*) ₹2,46,000 (*iv*) ₹2,31,000

Hidden Goodwill :

Sometimes, the value of goodwill is hidden in the question. In such cases, the amount of goodwill is calculated on the basis of total capital of the firm and the profit sharing ratio of the partners. For example, *A* and *B* are partners with capitals of ₹30,000 and ₹20,000 respectively. They admit *C* as a partner with 1/4th share. *C* is to contribute ₹24,000 as his capital. In such a case, the total capital of the firm, based on *C*'s share ought to be ₹24,000 $\times \frac{4}{1}$ = ₹96,000. But the combined capital of *A*, *B* and *C*

becomes only ₹74,000 (₹30,000 + ₹20,000 + ₹24,000). As such the value of total goodwill of the firm should be taken as ₹96,000 – ₹74,000 = ₹22,000.

ILLUSTRATION 62.

Karan and Varun were partners in a firm sharing profits and losses in the ratio of 1 : 2. Their fixed capitals were ₹2,00,000 and ₹3,00,000 respectively. On 1st April, 2016, Kishore was admitted as a new partner for 1/4th share in the profits. Kishore brought ₹2,00,000 for his capital which was to be kept fixed like the capitals of Karan and Varun. Kishore acquired his share of profit from Varun.

Calculate goodwill of the firm on Kishore's admission and the new profit sharing ratio of Karan, Varun and Kishore. Also, pass necessary Journal Entries.

(C.B.S.E. 2017, Delhi)

SOLUTION :

Calculation of Hidden Goodwill :

	₹
Total Capital of the new firm on the basis of	
Kishore's Capital $= 2{,}00{,}000 \times \frac{4}{1}$	= 8,00,000
Total Capital of Karan, Varun and Kishore : (₹2,00,000 + ₹3,00,000 + ₹2,00,000)	7,00,000
Value of Firm's Goodwill	1,00,000

Kishore's share $= \frac{1}{4}$ of ₹1,00,000 = ₹25,000

Calculation of New Profit Sharing Ratio :

Karan : $\frac{1}{3}$

Varun : $\frac{2}{3} - \frac{1}{4} = \frac{8-3}{12} = \frac{5}{12}$

Kishore : $\frac{1}{4}$

New Ratios : $\frac{1}{3} : \frac{5}{12} : \frac{1}{4}$ or $\frac{4:5:3}{12} = 4:5:3$

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Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2016 April 1	Bank A/c	Dr.		2,00,000	
	To Kishore's Capital A/c				2,00,000
	(Amount of Capital brought in by Kishore)				
April 1	Kishore's Current A/c	Dr.		25,000	
	To Varun's Current A/c				25,000
	(Kishore's share of goodwill credited to sacrificing partner's capital A/c)				

ILLUSTRATION 63.

Abhay and Beena are partners in a firm. They admit Chetan as a partner with 1/4th share in the profits of the firm. Chetan brings ₹2,00,000 as his share of capital. The value of the total assets of the firm is ₹5,40,000 and outside liabilities are valued at ₹1,00,000 on that date. Give the necessary entry to record goodwill at the time of Chetan's admission. Also show your working notes.

SOLUTION :

In this question, hidden goodwill is to be calculated.
Combined Capital of Abhay and Beena will be equal to the net worth of the business.

Net Worth = Sundry Assets – Outside Liabilities
= ₹5,40,000 – ₹1,00,000
= ₹4,40,000

Hence, combined capital of Abhay and Beena is ₹4,40,000.

CALCULATION OF HIDDEN GOODWILL

			₹
Based on Chetan's share, total capital of the new firm ought to be :			
	₹2,00,000 $\times \frac{4}{1}$ =		8,00,000
Less :	Net worth or Combined Capital of Abhay and Beena	4,40,000	
	Capital of Chetan	2,00,000	6,40,000
Value of Firm's Goodwill			1,60,000

Chetan's Share of Goodwill = ₹1,60,000 $\times \frac{1}{4}$ = ₹40,000.

JOURNAL ENTRIES

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bank A/c	Dr.		2,00,000	
	To Chetan's Capital A/c				2,00,000
	(Cash brought in by Chetan as his capital)				
	Chetan's Current A/c	Dr.		40,000	
	To Abhay's Capital A/c				20,000
	To Beena's Capital A/c				20,000
	(Credit given for goodwill to Abhay and Beena on Chetan's admission.)				

ILLUSTRATION 64.

Ramesh, Mahesh and Suresh were partners in a firm sharing profits in the ratio of 3 : 3 : 2. Their respective fixed capitals were : Ramesh ₹5,00,000; Mahesh ₹4,00,000 and Suresh ₹3,00,000. They admitted Govind as a new partner for $\frac{1}{5}$th share in the profits. Govind brought ₹4,00,000 as his capital and the necessary amount for goodwill premium. Their new profit sharing ratio will be 2 : 1 : 1 : 1.

Calculate the value of goodwill of the firm, showing your workings clearly. Pass necessary journal entries for the above transactions on Govind's admission.

(C.B.S.E. 2019, Chennai)

SOLUTION:

Calculation of hidden Goodwill of the firm :

I. Total capital of the firm based on new partner's capital :

$$4,00,000 \times \frac{5}{1} = ₹20,00,000$$

II. Combined capital of all partners = 5,00,000 + 4,00,000 + 3,00,000 + 4,00,000 = ₹16,00,000

III. Value of firm's Goodwill = 20,00,000 – 16,00,000 = ₹4,00,000

Govind's Share of Goodwill $= \frac{1}{5} \times 4,00,000 = ₹80,000$

Sacrificing Ratio :

Ramesh $= \frac{3}{8} - \frac{2}{5} = \frac{15-16}{40} = \frac{1}{40}$ Gain

Mahesh $= \frac{3}{8} - \frac{1}{5} = \frac{15-8}{40} = \frac{7}{40}$ Sacrifice

Suresh $= \frac{2}{8} - \frac{1}{5} = \frac{10-8}{40} = \frac{2}{40}$ Sacrifice

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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
(i)	Bank A/c	Dr.		4,80,000	
	To Govind's Capital A/c				4,00,000
	To Premium for Goodwill A/c				80,000
	(Capital and premium for goodwill brought in by Govind)				
(ii)	Premium for Goodwill A/c	Dr.		80,000	
	Remesh's Current A/c $(4,00,000 \times \frac{1}{40})$	Dr.		10,000	
	To Mehesh's Current A/c $(4,00,000 \times \frac{7}{40})$				70,000
	To Suresh's Current A/c $(4,00,000 \times \frac{2}{40})$				20,000
	(Adjustment made for treatment of goodwill)				

ILLUSTRATION 65.

Balance Sheet of *A* and *B* who share profits and losses in the ratio of 3 : 2 as at 31st August, 2022 was as follows :

Liabilities	₹	Assets	₹
Capital Accounts :		Fixed Assets	7,00,000
A	6,00,000	Stock	2,50,000
B	4,00,000	Debtors	2,00,000
Workmen Compensation Reserve	1,20,000	Cash	30,000
Sundry Creditors	80,000	Advertisement Expenditure (Deferred Revenue)	20,000
	12,00,000		12,00,000

They admit C as a partner for $\frac{1}{4}$th share in the profits of the firm which he acquires from A and B in the ratio of 2 : 3. C brings in ₹5,00,000 as his capital. There is a claim for Workmen Compensation amounting to ₹50,000. Ascertain the amount of goodwill and pass journal entries on admission of C.

SOLUTION:

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2022				
Aug. 1	Workmen Compensation Reserve A/c ... Dr.		1,20,000	
	To Liability for Workmen Compensation Claim A/c			50,000
	To *A*'s Capital A/c			42,000
	To *B*'s Capital A/c			28,000
	(Transfer of excess of Workmen Compensation Reserve to old partners in their old profit sharing ratio)			
Aug. 1	*A*'s Capital A/c ... Dr.		12,000	
	B's Capital A/c ... Dr.		8,000	
	To Advertisement Expenditure A/c			20,000
	(Transfer of accumulated loss to old partners in their old profit sharing ratio)			
Aug. 1	Bank A/c ... Dr.		5,00,000	
	To *C*'s Capital A/c			5,00,000
	(Amount brought in by *C* as his Capital)			
Aug. 1	*C*'s Current A/c ... Dr.		1,12,500	
	To *A*'s Capital A/c			45,000
	To *B*'s Capital A/c			67,500
	(*C*'s share of goodwill credited to *A* and *B* in their sacrificing ratio of 2 : 3)			

Working Note :

Calculation of Hidden Goodwill :

			₹
Total of Capital of the new firm on the basis of *C*'s Capital : ₹5,00,000 × $\frac{4}{1}$			20,00,000
Less:	Net worth of new firm :		
	Adjusted Capital of *A* (₹6,00,000 + ₹42,000 – ₹12,000)	6,30,000	
	Adjusted Capital of *B* (₹4,00,000 + ₹28,000 – ₹8,000)	4,20,000	
	Capital of *C*	5,00,000	15,50,000
	Value of Firm's Goodwill		4,50,000

C's share of Goodwill = ₹4,50,000 × $\frac{1}{4}$ = 1,12,500.

ILLUSTRATION 66.

Following is the balance sheet of *A* and *B* who share profits and losses in the ratio of 2 : 1 as at 31st March, 2022 :

Liabilities	₹	*Assets*	₹
A's Capital	3,00,000	Cash and Bank	25,000
B's Capital	2,00,000	Sundry Debtors	2,00,000

Reserves	70,000	Stock	2,15,000
Profit and Loss A/c	50,000	Plant and Machinery	1,80,000
Sundry Creditors	80,000	Goodwill	60,000
		Advertisement Expenditure	20,000
	7,00,000		7,00,000

They admit *C* as a partner from 1st April 2022 with 1/4th share in the profits of the firm. *C* brings ₹3,20,000 as his Capital. Give journal entries for the adjustment of goodwill.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2022					
April 1	*A*'s Capital A/c	Dr.		40,000	
	B's Capital A/c	Dr.		20,000	
	To Goodwill A/c				60,000
	(Existing goodwill written off in old ratio of 2 : 1)				
April 1	*C*'s Current A/c	Dr.		1,05,000	
	To *A*'s Capital A/c (₹1,05,000 × 2/3)				70,000
	To *B*'s Capital A/c (₹1,05,000 × 1/3)				35,000
	(*C*'s share of goodwill credited to sacrificing partner's capital accounts in 2 : 1)				

Working Note :

Calculation of Hidden Goodwill :

			₹
Total Capital of the new firm on the basis of *C*'s Capital : ₹3,20,000 × $\frac{4}{1}$			12,80,000
Less :	Net worth of the new firm :		
	Adjusted Capitals of *A* and *B* (₹3,00,000 + ₹2,00,000 + ₹70,000 for Reserves + ₹50,000 for P & L – ₹60,000 for existing goodwill – ₹20,000 for Adv. Expenditure)	5,40,000	
	Capital of *C*	3,20,000	8,60,000
	Value of Firm's Goodwill		4,20,000

C's share of Goodwill = ₹4,20,000 × $\frac{1}{4}$ = ₹1,05,000.

ILLUSTRATION 67.

Aditi and Parul are partners in a firm with capitals of ₹35,000 each. They shared profits and losses in the ratio of 3 : 1.

On 1st April, 2017, they admit Chanda into their partnership with 1/5th share in the profits.

Chanda brings in ₹40,000 as her capital and also brings her share of goodwill in cash.

Her share of goodwill is calculated on the basis of her capital contribution and her share of profits in the firm.

At the time of Chanda's admission :

(*a*) The firm had a Workmen Compensation Reserve of ₹60,000 against which there was a claim of ₹20,000.

(*b*) Creditors of ₹8,000 were paid by Aditi privately for which she is not to be reimbursed.

(*c*) There was no change in the value of other assets and liabilities.

You are required to, on the date of Chanda's admission :

(*i*) Calculate the goodwill of the firm. (Show the workings clearly).

(*ii*) Pass the necessary journal entries to record the above transactions.

(I.S.C. 2019)

SOLUTION :

			₹
Calculation of hidden goodwill of the firm :			
Total Capital of the firm based on Chanda's Capital = 5 × 40,000			2,00,000
Less :	Net worth of the business :		
	Adjusted Capitals of all the partners		
	(Capital + Workmen Compensation Reserve + Creditors)		
	Aditi 35,000 + 30,000 + 6,000 =	71,000	
	Parul 35,000 + 10,000 + 2,000 =	47,000	
	Chanda	40,000	1,58,000
	Hidden Goodwill		42,000

Chanda's share of Goodwill = $42{,}000 \times \frac{1}{5}$ = ₹8,400

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2017 April 1	Workmen Compensation Reserve A/c	Dr.		60,000	
	To Workmen Compensation Claim A/c				20,000
	To Aditi's Capital A/c				30,000
	To Parul's Capital A/c				10,000
	(Excess of Workmen Compensation Reserve credited in old ratio)				
April 1	Creditors A/c	Dr.		8,000	
	To Revaluation A/c				8,000
	(Gain on creditors being paid by a partner and not to be reimbursed)				
April 1	Revaluation A/c	Dr.		8,000	
	To Aditi's Capital A/c				6,000
	To Parul's Capital A/c				2,000
	(Gain on revaluation transferred in old ratio)				
April 1	Bank A/c	Dr.		48,400	
	To Chanda's Capital A/c				40,000
	To Premium for Goodwill A/c				8,400
	(Capital and premium for goodwill contributed by Chanda)				

April 1	Premium for Goodwill A/c Dr.		8,400	
	To Aditi's Capital A/c			6,300
	To Parul's Capital A/c			2,100
	(Premium for goodwill credited to old partners in sacrificing ratio of 3 : 1)			

ILLUSTRATION 68.

Deepika and Rajshree are partners in a firm sharing profits and losses in the ratio of 3 : 2. On 31st March, 2022, their Balance Sheet was as under :

Liabilities		₹	*Assets*		₹
Sundry Creditors		16,000	Cash in Hand		1,200
Public Deposits		61,000	Cash at Bank		2,800
Bank Overdraft		6,000	Stock		32,000
Outstanding Liabilities		2,000	Prepaid Insurance		1,000
Capital Accounts :			Sundry Debtors	28,800	
Deepika	48,000		*Less* : Provision for		
Rajshree	40,000	88,000	Doubtful Debts	800	28,000
			Plant and Machinery		48,000
			Land and Building		50,000
			Furniture		10,000
		1,73,000			1,73,000

On 1st April, 2022, the partners decide to admit Anshu as a partner on the following terms :

(*i*) The new profit-sharing ratio of Deepika, Rajshree and Anshu will be 5 : 3 : 2, respectively.

(*ii*) Anshu shall bring ₹32,000 as his capital.

(*iii*) Anshu is unable to bring in any cash for his share of goodwill. Partners, therefore, decide to calculate goodwill on the basis of Anshu's share in the profits and the capital contribution made by him to the firm.

(*iv*) Plant and Machinery would be increased by ₹12,000.

(*v*) Stock would be increased to ₹40,000.

(*vi*) Provision for Doubtful Debts is to be maintained at ₹4,000. Value of Land and Building has appreciated by 20%. Furniture has depreciated by 10%.

(*vii*) There is an additional liability of ₹8,000 being outstanding salary payable to employees of the firm. This liability is not included in the outstanding liabilities, stated in the above Balance Sheet. Partners decide to show this liability in the books of accounts of the reconstituted new firm.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet of Deepika, Rajshree and Anshu.

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Provision for Doubtful debts		3,200	By Plant and Machinery	12,000
To Furniture		1,000	By Stock	8,000
To Outstanding Salary		8,000	By Land and Building	10,000
To Profit transferred to :				
Deepika's Capital A/c (3/5)	10,680			
Rajshree's Capital A/c (2/5)	7,120	17,800		
		30,000		30,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*Deepika*	*Rajshree*	*Anshu*	*Particulars*	*Deepika*	*Rajshree*	*Anshu*
	₹	₹	₹		₹	₹	₹
To Balance c/d	60,900	49,340	32,000	By Balance b/d	48,000	40,000	—
				By Revaluation	10,680	7,120	—
				By Anshu's Current A/c[(2)]	2,220	2,220	—
				By Bank A/c	—		32,000
	60,900	49,340	32,000		60,900	49,340	32,000

OPENING BALANCE SHEET *as at 1st April, 2022*

Liabilities		₹	*Assets*		₹
Sundry Creditors		16,000	Cash in Hand		1,200
Public Deposits		61,000	Bank Balance[(1)]		28,800
Outstanding Liabilities		10,000	Stock		40,000
Capital Accounts :			Prepaid Insurance		1,000
Deepika	60,900		Sundry Debtors	28,800	
Rajshree	49,340		*Less* : Provison	4,000	24,800
Anshu	32,000	1,42,240	Plant and Machinery		60,000
			Land and Buildings		60,000
			Furniture		9,000
			Anshu's Current A/c		4,440
		2,29,240			2,29,240

Notes : (1) Bank Balance : ₹2,800 + ₹32,000 – Bank Overdraft ₹6,000 = ₹28,800.

(2) In this question the amount of goodwill is hidden, which will be found out as below :

Based on Anshu's share of profit, the total capital of the firm should be ₹

$₹32,000 \times \frac{10}{2}$ = 1,60,000

Less : Capital of Deepika (₹48,000 + Profit on Revaluation ₹10,680) = 58,680

Capital of Rajshree (₹40,000 + Profit on Revaluation ₹ 7,120) = 47,120

Capital of Anshu	= 32,000	1,37,800
Value of Goodwill :		22,200

Anshu's share of Goodwill $= 22{,}200 \times \frac{2}{10} =$ ₹4,440

Anshu's Current A/c will be debited by her share of goodwill *i.e.* ₹4,440 and Deepika and Rajshree will be credited in their sacrificing ratio *i.e.* equally.

Sacrifice made by Deepika $= \frac{3}{5} - \frac{5}{10} = \frac{1}{10}$

Sacrifice made by Rajshree $= \frac{2}{5} - \frac{3}{10} = \frac{1}{10}$

When the new partner brings in proportionate capital :— Sometimes the capital of the new partner is not given in the question. He may be required to bring in proportionate capital. In such cases the new partner's capital will be calculated on the basis of the capitals of the old partners remaining after all adjustments and revaluation.

For example, the Capitals of A and B after all the adjustments and revaluations are ₹24,000 and ₹16,000 respectively. They admitted C as a new partner with 1/5th share in the profits. C's capital will be calculated as follows :

Share of A and B (after giving $\frac{1}{5}$ th share to C) $= \frac{4}{5}$

Thus, if for $\frac{4}{5}$ th share of profits the Combined Capital of A and $B =$ ₹40,000

then total capital of the firm $= 40{,}000 \times \frac{5}{4} =$ ₹50,000

$\therefore$ C's Capital for $\frac{1}{5}$ th share of profits $= 50{,}000 \times \frac{1}{5} =$ ₹10,000

$\therefore$ C will bring in ₹10,000 as his Capital.

New Partner's Capital not given :—

ILLUSTRATION 69.

The following is the Balance Sheet of A and B as at 31st March, 2022, who share profits in the ratio of 2 : 1.

Liabilities	₹	*Assets*		₹
Bank Overdraft	15,000	Sundry Debtors	40,000	
Reserve Fund	12,000	*Less* : Provision	3,600	36,400
Sundry Creditors	20,000	Stock		20,000
Capitals : A	40,000	Building		25,000
B	30,000	Patents		2,000
		Machinery		33,600
	1,17,000			1,17,000

They admitted C into partnership on 1st April, 2022. New profit sharing ratio is agreed as $\frac{3}{6} : \frac{2}{6} : \frac{1}{6}$. C brings in proportionate capital after the following adjustments:

(1) C brings in ₹10,000 in cash as his share of Goodwill.

(2) Provision for doubtful debts is to be reduced by ₹2,000.

(3) There is an old typewriter valued ₹2,600. It does not appear in the books of the firm. It is now to be recorded.

(4) Patents are valueless.

(5) 2 % discount is to be received from creditors.

Prepare Revaluation A/c, Capital A/cs and the opening Balance Sheet.

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Patents	2,000	By Provision for Doubtful Debts	2,000
To Profit transferred to :		By Typewriter	2,600
A's Capital A/c	2,000	By Provision for Discount on	
B's Capital A/c	1,000	Creditors	400
	5,000		5,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Bal. c/d	60,000	35,000		By Bal. b/d	40,000	30,000	
				By Reserve Fund	8,000	4,000	
				By Revaluation	2,000	1,000	
				By Premium for Goodwill A/c[(1)]	10,000		
	60,000	35,000			60,000	35,000	
To Bal. c/d	60,000	35,000	19,000	By Bal. b/d	60,000	35,000	—
				By Bank			19,000[(2)]
	60,000	35,000	19,000		60,000	35,000	19,000

OPENING BALANCE SHEET

as at 1st April, 2022

Liabilities		₹	*Assets*		₹
Sundry Creditors	20,000		Bank[(3)]		14,000
Less : Provision	400	19,600	Sundry Debtors	40,000	
Capitals :			*Less* : Provision	1,600	38,400
A		60,000	Stock		20,000
B		35,000	Building		25,000
C		19,000	Machinery		33,600
			Typewriter		2,600
		1,33,600			1,33,600

Hints : (1) Sacrifice Ratio = Old Ratio – New Ratio

Sacrifice by A $= \text{Old}\frac{2}{3} - \text{New}\frac{3}{6} = \frac{1}{6}$

Sacrifice by B $= \text{Old}\frac{1}{3} - \text{New}\frac{2}{6} = 0$

Since B has not made any sacrifice, the entire amount of premium for goodwill brought in by C will be credited to A.

(2) C's Capital is not given in the question. He will bring in capital proportionate to his share of profits. C is given 1/6th share of profits, balance 5/6th share is shared by A and B. Total capital of A and B after all adjustments is ₹60,000 + ₹35,000 = ₹95,000.

Thus for $\frac{5}{6}$th share of profits the Capital = 95,000

Then the total Capital of the Firm $= 95{,}000 \times \frac{6}{5} =$ ₹1,14,000

∴ C's Capital for $\frac{1}{6}$th share of profits $= 1{,}14{,}000 \times \frac{1}{6} =$ ₹ 19,000

(3) Calculation of Balance at Bank :

		₹
Amount of Cash brought in by C as goodwill	=	10,000
Amount of Cash brought in by C as capital	=	19,000
		29,000
(–) Bank Overdraft		15,000
Balance at Bank		14,000

ILLUSTRATION 70.

Given below is the Balance Sheet of Charu and Divya who are partners in a firm sharing profits in the ratio of 3 : 2.

Liabilities		₹	*Assets*	₹
Sundry Creditors		3,00,000	Land & Buildings	4,00,000
Profit and Loss Account		1,00,000	Plant & Machinery	3,00,000
Capital Accounts :			Stock	70,000
Charu	4,00,000		Debtors	1,80,000
Divya	2,00,000	6,00,000	Bank	50,000
		10,00,000		10,00,000

On that date Esha is admitted as a partner on the following terms:

(*a*) Charu gives 1/3rd of her share while Divya gives 1/10th from her share to Esha.

(*b*) Goodwill is valued at 2 years' purchase of the average profits of the last 5 years, which were ₹50,000 (Loss); ₹1,20,000; ₹10,000 (Loss), ₹3,00,000 and ₹3,40,000 respectively. Esha does not bring her share of goodwill in cash.

(*c*) Esha brings in capital in proportion to her share of profit in the firm.

Pass necessary journal entries.

SOLUTION :

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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
				₹	₹
	Profit & Loss A/c	Dr.		1,00,000	
	To Charu's Capital A/c				60,000
	To Divya's Capital A/c				40,000
	(Transfer of Profit & Loss balance to old partner's capital accounts)				
	Esha's Current A/c	Dr.		84,000	
	To Charu's Capital A/c				56,000
	To Divya's Capital A/c				28,000
	(Adjustment for goodwill in sacrificing ratio of 2 : 1)				
	Bank A/c	Dr.		3,36,000	
	To Esha's Capital A/c				3,36,000
	(Proportionate capital brought in by Esha)				

Working Notes :

(1) Calculation of Sacrificing Ratios :

Share surrendered by Charu $= \frac{3}{5} \times \frac{1}{3} = \frac{1}{5}$

Share surrendered by Divya $= \frac{1}{10}$

Sacrificing Ratio $= \frac{1}{5} : \frac{1}{10} = 2 : 1$

(2) Calculation of Esha's share :

$\frac{1}{5} + \frac{1}{10} = \frac{2+1}{10} = \frac{3}{10}$

(3) Valuation of Goodwill :

Average Profit $= \frac{(-)\ 50,000 + 1,20,000\ (-)\ 10,000 + 3,00,000 + 3,40,000}{5}$

$=$ ₹1,40,000

Goodwill at 2 year's purchase $= 1,40,000 \times 2 =$ ₹2,80,000

Esha's share of Goodwill $= 2,80,000 \times \frac{3}{10} =$ ₹84,000

(4) Charu's Capital : ₹4,00,000 + 60,000 + 56,000 = 5,16,000

Divya's Capital : ₹2,00,000 + 40,000 + 28,000 = 2,68,000

7,84,000

For $\frac{7}{10}$th share of Profits the Capital $= 7,84,000$

Total Capital of the Firm $= 7,84,000 \times \frac{10}{7} = 11,20,000$

Esha's Capital for $\frac{3}{10}$th share $= 11,20,000 \times \frac{3}{10} = 3,36,000$

ILLUSTRATION 71.

A and *B* are partners in a firm sharing profits and losses in the ratio 3 : 1. They admit *C* for 1/4 share on 31st March 2014 when their Balance Sheet was as follows :

Liabilities	₹	*Assets*		₹
Employee's Provident Fund	17,000	Stock		15,000
Workmen's Compensation		Sundry Debtors	50,000	
Reserve	6,000	*Less* : Provision for		
Investment Fluctuation Reserve	4,100	Doubtful debts	2,000	48,000
Capitals : *A*	54,000	Investments		7,000
B	35,000	Cash		6,100
		Goodwill		40,000
	1,16,100			1,16,100

The following adjustments were agreed upon :

(*a*) *C* brings in ₹16,000 as goodwill and proportionate capital.

(*b*) Bad debts amounted to ₹3,000.

(*c*) Market value of investments is ₹4,500.

(*d*) Liability on account of workmen's compensation reserve amounted to ₹2,000.

Prepare Revaluation A/c and Partner's Capital A/cs.

(C.B.S.E. Sample Question Paper, 2015)

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Bad Debts A/c (Note 1)	1,000	By Loss on Revaluation Transferred to :	
		A's Capital A/c	750
		B's Capital A/c	250
	1,000		1,000

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*A* ₹	*B* ₹	*C* ₹	*Particulars*	*A* ₹	*B* ₹	*C* ₹
To Goodwill (Written off)	30,000	10,000		By Bal. b/d	54,000	35,000	—
To Revaluation (Loss)	750	250		By Workmen's Compensation Reserve	3,000	1,000	
To Balance c/d	39,450	30,150		By Investment Fluctuation Res.	1,200	400	
				By Premium for Goodwill	12,000	4,000	
	70,200	40,400			70,200	40,400	
To Balance c/d	39,450	30,150	23,200	By Balance b/d	39,450	30,150	

				By Bank			23,200
	39,450	30,150	23,200		39,450	30,150	23,200

Working Notes :

(1) Entry for Bad Debts :

(*i*) Bad Debts A/c	Dr.	3,000	
To Sundry Debtors A/c			3,000
(*ii*) Provision for Doubtful Debts A/c	Dr.	2,000	
Revaluation A/c	Dr.	1,000	
To Bad Debts A/c			3,000

(2) Workmen's Compensation Reserve	Dr.	6,000	
To Liability for Workmen's Compensation Claim			2,000
To *A*'s Capital A/c			3,000
To *B*'s Capital A/c			1,000
(3) Investment Fluctuation Reserve A/c	Dr.	4,100	
To Investments A/c			2,500
To *A*'s Capital A/c			1,200
To *B*'s Capital A/c			400

(4) *C* is given 1/4th share, balance 3/4th share is shared by *A* and *B*. Total Capital of *A* and *B* after all adjustments is ₹39,450 + ₹30,150 = ₹69,600.

Thus, for 3/4th share of profits the capital is ₹69,600

Then, Total Capital of the firm $= 69,600 \times \frac{4}{3} =$ ₹92,800

$\therefore$ *C*'s Capital for $\frac{1}{4}$th share $= 92,800 \times \frac{1}{4} =$ ₹23,200

ILLUSTRATION 72.

Madhuri and Arsh were partners in a firm sharing profits and losses in the ratio of 3 : 1. Their Balance Sheet as at 31st March, 2019 was as follows :

BALANCE SHEET OF MADHURI AND ARSH

as at 31st March, 2019

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Capitals :			Machinery		4,70,000
Madhuri	3,00,000		Investments		1,10,000
Arsh	2,00,000	5,00,000	Debtors	1,20,000	
Workmen's Compensation			*Less* : Provision for		
Reserve		60,000	Doubtful Debts	10,000	1,10,000
Creditors		1,90,000	Stock		1,40,000
Employees' Provident Fund		1,10,000	Cash		30,000
		8,60,000			8,60,000

On 1st April, 2019, they admitted Jyoti into partnership for $\frac{1}{4}$th share in the profits of the firm. Jyoti brought proportionate capital and ₹40,000 as her share of goodwill premium.

The following terms were agreed upon :

(i) Provision for doubtful debts was to be maintained at 10% on debtors.

(ii) Stock was undervalued by ₹10,000.

(iii) An old customer whose account of ₹25,000 was written off as bad, paid ₹15,000 in full settlement.

(iv) 20% of the investments were taken over by Arsh at book value.

(v) Claim on account of workmen's compensation amounted to ₹70,000.

(vi) Creditors included a sum of ₹27,000 which was not likely to be claimed.

Prepare Revaluation Account, Partner's Capital Accounts, and the Balance Sheet of the reconstituted firm. *(C.B.S.E. 2020, Lucknow, Kolkata)*

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars	*Amount*	*Particulars*	*Amount*
	₹		₹
To Provision for Doubtful Debts A/c	2,000	By Stock A/c	10,000
To Workmen's Compensation Claim A/c	10,000	By Bad Debts Recovered A/c[(1)]	15,000
To Profit transferred to :		By Creditors A/c	27,000
Madhuri's Capital A/c 30,000			
Arsh's Capital A/c 10,000	40,000		
	52,000		52,000

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*Madhuri*	*Arsh*	*Jyoti*	*Particulars*	*Madhuri*	*Arsh*	*Jyoti*
	₹	₹	₹		₹	₹	₹
To Investments A/c		22,000	—	By Balance b/d	3,00,000	2,00,000	—
To Balance c/d	3,60,000	1,98,000	—	By Premium for Goodwill A/c	30,000	10,000	—
				By Revaluation A/c	30,000	10,000	—
	3,60,000	2,20,000			3,60,000	2,20,000	
To Balance c/d	3,60,000	1,98,000	1,86,000	By Balance b/d	3,60,000	1,98,000	—
				By Bank A/c[(2)]			1,86,000
	3,60,000	1,98,000	1,86,000		3,60,000	1,98,000	1,86,000

BALANCE SHEET OF MADHURI, ARSH AND JYOTI
as at 31st March, 2019

Liabilities		₹	Assets		₹
Capitals :			Machinery		4,70,000
Madhuri	3,60,000		Investments		88,000
Arsh	1,98,000		Debtors	1,20,000	
Jyoti	1,86,000	7,44,000	*Less* : Provision for		
Workmen's Compensation Claim		70,000	Doubtful Debts	12,000	1,08,000
Creditors		1,63,000	Stock		1,50,000
Employees Provident Fund		1,10,000	Cash and Bank(3)		2,71,000
		10,87,000			10,87,000

Working Notes :

(1) Entries for Bad Debts recovered :

Bank A/c	Dr.	15,000	
To Bad Debts Recovered A/c			15,000
Bad Debts Recovered A/c	Dr.	15,000	
To Revaluation A/c			15,000

There will be no effect of the bad debts recovered on the amount of debtors appearing in the balance sheet.

(2) Total Capital of Madhuri and Arsh after adjustments
$= ₹3,60,000 + ₹1,98,000 = ₹5,58,000$

Jyoti is given $\frac{1}{4}$th share of profits.

Thus, for $\frac{3}{4}$th share of profits the Capital = ₹5,58,000

Total Capital of the Firm $= 5,58,000 \times \frac{4}{3} = ₹7,44,000$

Jyoti's Capital for $\frac{1}{4}$th share $= 7,44,000 \times \frac{1}{4} = ₹1,86,000$

(3) Cash & Bank Balance = 30,000 + 15,000 (Bad Debts Recovered) + 1,86,000 + 40,000 = ₹2,71,000

ILLUSTRATION 73.

A and *B* are partners and the profit is divided as follows : $\frac{1}{2}$ to *A*; $\frac{1}{3}$ to *B* and $\frac{1}{6}$ carried to a Reserve Account. They admit *C* as a partner on 1st April, 2018 at which date the Balance Sheet of the firm was as under :

Liabilities		₹	Assets	₹
Creditors		1,60,000	Cash at Bank	20,000
Outstanding Expenses		12,000	Debtors	2,20,000
Reserve		90,000	Stock	1,80,000
Capital A/cs :			Plant and Machinery	1,50,000
A	3,18,000		Buildings	2,00,000
B	2,00,000	5,18,000	Advertisement Expenditure	10,000
		7,80,000		7,80,000

Following terms were agreed upon :

(i) Stock is undervalued by 10%.

(ii) Depreciation of ₹30,000 had been omitted on plant and machinery for the year ended 31st March, 2018.

(iii) Creditors include a Contingent liability of ₹50,000 which has been decided by the Court at ₹43,000.

(iv) In respect of debtors, the following debts proved bad or doubtful :
₹15,000 due from Ram — bad to the full extent;
₹20,000 due from Shyam — insolvent, estate expected to pay only 40%.

(v) Goodwill of the firm is valued at ₹60,000. However, *C* is unable to bring his share of goodwill in Cash.

(vi) *C* is given $\frac{1}{5}$th share of profits which he acquires equally from *A* and *B*. *C* is to bring in Capital proportionate to his share of profits in the firm.

You are required to prepare Revaluation Account, Capital Accounts and the new Balance Sheet of the firm.

SOLUTION :

Profit Sharing Ratio of *A* and *B* $= \frac{1}{2} : \frac{1}{3} = \frac{3 : 2}{6} = 3 : 2$

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	Particulars		₹
To Plant and Machinery	30,000	By Stock (Note 1)		20,000
To Debtors (Bad Debts)	15,000	By Creditors		7,000
To Provision for Doubtful Debts	12,000	By Loss transferred to		
		A's Capital A/c	18,000	
		B's Capital A/c	12,000	30,000
	57,000			57,000

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	A	B	C	Particulars	A	B	C
	₹	₹	₹		₹	₹	₹
To Advertisement Exp.	6,000	4,000		By Balance b/d	3,18,000	2,00,000	
To Revaluation	18,000	12,000		By Reserve	54,000	36,000	
To Balance c/d	3,54,000	2,26,000		By C's Current A/c (Note 2)	6,000	6,000	
	3,78,000	2,42,000			3,78,000	2,42,000	
To Balance c/d	3,54,000	2,26,000	1,45,000	By Balance b/d	3,54,000	2,26,000	
				By Bank (Note 3)			1,45,000
	3,54,000	2,26,000	1,45,000		3,54,000	2,26,000	1,45,000

BALANCE SHEET *as at 1st April, 2018*

Liabilities		₹	*Assets*		₹
Creditors		1,53,000	Cash at Bank		1,65,000
Outstanding Expenses		12,000	Debtors	2,20,000	
Capital A/cs			*Less* : Bad Debts	15,000	
A	3,54,000			2,05,000	
B	2,26,000		*Less* : Provision	12,000	1,93,000
C	1,45,000	7,25,000	Stock		2,00,000
			Plant and Machinery		1,20,000
			Buildings		2,00,000
			C's Current A/c		12,000
		8,90,000			8,90,000

Working Notes :

		₹
(1) Full Value of Stock	$= 1,80,000 \times \frac{100}{90} =$	2,00,000
Value shown in Balance Sheet		1,80,000
Stock to be increased by :		20,000

(2) *C*'s share of Goodwill $= 60,000 \times \frac{1}{5} =$ ₹12,000

A's share of Goodwill $= 12,000 \times \frac{1}{2} =$ ₹ 6,000

B's share of Goodwill $= 12,000 \times \frac{1}{2} =$ ₹ 6,000

C's share of goodwill has been debited to his Current Account instead of his Capital Account. Hence, entry for goodwill will be :

C's Current A/c	Dr.	12,000	
To *A*'s Capital A/c			6,000
To *B*'s Capital A/c			6,000
(Goodwill Credited to *A* and *B* in sacrificing ratio)			

(3) Calculation of *C*'s Capital :

C's share in profit $= \frac{1}{5}$

For $\frac{4}{5}$th share, combined Capital of *A* and *B* = 3,54,000 + 2,26,000 = 5,80,000

Total Capital of the new firm $= 5,80,000 \times \frac{5}{4} = 7,25,000$

C's Capital $= 7,25,000 \times \frac{1}{5} =$ ₹1,45,000

ILLUSTRATION 74.

A and *B* are partners sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as at 31st March, 2018 stood as under :

Liabilities	₹	*Assets*	₹
Capitals :		Machinery	66,000
A	70,000	Furniture	30,000

B	60,000	Investments		40,000
General Reserve	20,000	Stock		46,000
Bank Loan	18,000	Debtors	38,000	
Creditors	72,000	*Less* : Provision	4,000	34,000
		Cash		24,000
	2,40,000			2,40,000

On 1st April, 2018 admitted *C* for 25% share in profits on following terms :

(*i*) *C* brings in Capital proportionate to his share after all adjustments and ₹8,000 for goodwill out of his share of ₹14,000.

(*ii*) Depreciate furniture by 10%.

(*iii*) Half of investments were to be taken over by *A* and *B* in their profit sharing ratio and remaining valued at ₹26,000.

(*iv*) New ratio will be 3 : 3 : 2.

Prepare Revaluation Account, Capital Accounts and Balance Sheet after *C*'s admission.

SOLUTION :

Books of Firm

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Furniture		3,000	By Investments	6,000
To Profit transferred to				
A's Capital A/c	1,800			
B's Capital A/c	1,200	3,000		
		6,000		6,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A* ₹	*B* ₹	*C* ₹	*Particulars*	*A* ₹	*B* ₹	*C* ₹
To Investments	12,000	8,000	—	By Balance b/d	70,000	60,000	—
To Balance c/d	84,400	62,600	49,000	By General Reserve	12,000	8,000	—
				By Revaluation A/c Profit	1,800	1,200	—
				By Premium for Goodwill A/c	7,200	800	—
				By *C*'s Current A/c[(1)]	5,400	600	
				By Cash A/c			49,000
	96,400	70,600	49,000		96,400	70,600	49,000

BALANCE SHEET OF *A*, *B* AND *C*
as at 1st April, 2018

Liabilities	₹	Assets		₹
Capital Accounts :		Machinery		66,000
A	84,400	Furniture		27,000
B	62,600	Investments		26,000
C	49,000	Stock		46,000
Bank Loan	18,000	Debtors	38,000	
Creditors	72,000	*Less :* Provision for Doubtful Debts	4,000	34,000
		C's Current A/c		6,000
		Cash		81,000
	2,86,000			2,86,000

Working Notes :

(1) Calculation of Sacrificing Ratio :

$$A = \frac{3}{5} - \frac{3}{8} = \frac{24-15}{40} = \frac{9}{40}$$

$$B = \frac{2}{5} - \frac{3}{8} = \frac{16-15}{40} = \frac{1}{40}$$

Sacrificing Ratio = 9 : 1

Journal Entries for Goodwill :

		Dr.	Cr.
Cash A/c	Dr.	8,000	
To Premium for Goodwill A/c			8,000
(₹8,000 brought in by *C* for his share of goodwill out of ₹14,000)			
Premium for Goodwill A/c	Dr.	8,000	
To *A*'s Capital A/c			7,200
To *B*'s Capital A/c			800
(Premium for goodwill credited to *A* and *B* in their sacrificing ratio 9 : 1)			
C's Current A/c*	Dr.	6,000	
To *A*'s Capital A/c			5,400
To *B*'s Capital A/c			600
(Unpaid amout of goodwill credited to *A* and *B* in their sacrificing ratio 9 : 1)			

**C*'s Current A/c has been debited instead of his Capital Account.

(2) Capital brought in by *C*

C's share in profit = 25% or $\frac{1}{4}$

For $\frac{3}{4}$th share, combined capital of *A* and *B* are (₹84,400 + ₹62,600) ₹1,47,000

∴ Total Capital of firm $= ₹1,47,000 \times \frac{4}{3} = ₹1,96,000$

∴ *C*'s share in total capital $= ₹1,96,000 \times \frac{1}{4} = ₹\ 49,000$

ILLUSTRATION 75.

Given below is the Balance Sheet of Mr. Raymond as at 31st March, 2022 :

Liabilities	₹	*Assets*	₹
Capital	4,00,000	Plant and Machinery	1,05,000
Bank Overdraft	60,000	Building	1,95,000
Bills Payable	15,000	Furniture and Fixtures	50,000
Creditors	50,000	Investments	25,000
		Stock	45,000
		Sundry Debtors	40,000
		Cash at Bank	65,000
	5,25,000		5,25,000

Raymond with a view to extend his business, negotiated with Simon, who entered into the partnership on 1st April, 2022 to share profits and losses in the ratio of 2 : 1.

The arrangement made between them was as follows :

(*a*) Furniture and fixtures are to be taken at 90% of their value.

(*b*) Buildings and Plant and Machinery are to be taken at an appreciated value of 10%.

(*c*) ₹4,000 of Sundry Debtors are bad and there was doubtful amount of ₹1,500.

(*d*) A creditor for ₹3,000 is not traceable for a number of years and the amount is to be written off.

(*e*) Stock is to be taken at ₹42,000.

(*f*) Investments and bank overdraft not to be taken over by the new partnership. An amount of ₹40,000 to be brought in by Simon as premium for goodwill.

Simon to bring in further cash to make his capital equal to that of Raymonds after making therein the adjustments mentioned above.

Make the necessary Journal entries to record the above transactions and prepare the opening Balance Sheet of the partnership.

SOLUTION : JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2022					
April 1	Revaluation A/c	Dr.		13,500	
	To Furniture and Fixtures A/c				5,000
	To Sundry Debtors A/c (Bad debts)				4,000
	To Provision for Doubtful Debts A/c				1,500
	To Stock A/c				3,000
	(Amount of decrease in the value of assets as a result of revaluation)				
	Building A/c	Dr.		19,500	
	Plant and Machinery A/c	Dr.		10,500	
	Creditors A/c	Dr.		3,000	
	To Revaluation A/c				33,000
	(Increase in value of assets and reduction in the value of liability of creditors)				

Revaluation A/c Dr. To Raymond's Capital A/c (Profit on revaluation credited to Raymonds' Capital)		19,500	19,500
Raymond's Capital A/c Dr. To Investments A/c (Investments not taken over by the partnership)		25,000	25,000
Bank Overdraft A/c Dr. To Raymond's Capital A/c (Bank overdraft not taken over by the partnership)		60,000	60,000
Bank A/c Dr. To Simon's Capital A/c To Premium for Goodwill A/c (Amount introduced by Simon : ₹4,94,500 for capital and ₹40,000 as premium for goodwill)		5,34,500	4,94,500 40,000
Premium for Goodwill A/c Dr. To Raymond's Capital A/c (Premium for goodwill credited to Raymond's capital)		40,000	40,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*Raymond*	*Simon*	*Particulars*	*Raymond*	*Simon*
	₹	₹		₹	₹
To Investments	25,000		By Balance b/d	4,00,000	
To Balance c/d	4,94,500	4,94,500	By Revaluation	19,500	
			By Bank Overdraft	60,000	
			By Premium for Goodwill A/c	40,000	
			By Bank A/c		4,94,500
	5,19,500	4,94,500		5,19,500	4,94,500

BALANCE SHEET
as at 1st April, 2022

Liabilities		₹	*Assets*		₹
Capital Accounts :			Plant and Machinery		1,15,500
Raymond	4,94,500		Building		2,14,500
Simon	4,94,500	9,89,000	Furniture and Fixtures		45,000
Bills Payable		15,000	Stock		42,000
Creditors		47,000	Sundry Debtors	36,000	
			Less : Provision for doubtful Debts	1,500	34,500
			Cash at Bank		5,99,500
		10,51,000			10,51,000

Adjustment of Old Partner's Capital Accounts on the basis of new partner's capital :

Sometimes, on the admission of a new partner it is decided that the capitals of the old partners will be adjusted on the basis of new partner's capital to make them

proportionate to their share of profits. In such questions, first of all the entire Capital of the new firm should be determined on the basis of new partner's capital. Then the Capital of each partner is ascertained by dividing the total Capital according to his profit sharing ratio.

If the existing capital of any partner is in excess of his newly calculated capital, the excess amount is either paid off immediately or credited to his current account. Following entry is passed for this purpose :

(i) Old Partner's Capital A/c ... Dr.
To Bank A/c or Partner's Current A/c

(ii) If the existing Capital of any partner is less than his newly calculated capital :
Bank A/c or Partner's Current A/c ... Dr.
To Old Partner's Capital A/c

ILLUSTRATION 76.

The following is the balance sheet of *A, B* and *C* sharing profits and losses in proportion of 6 : 5 : 3 respectively :—

Liabilities		₹	*Assets*	₹
Creditors		18,900	Cash	1,890
Bills Payable		6,300	Debtors	26,460
General Reserve		10,500	Stock	29,400
Capitals :—			Furniture	7,350
A	35,400		Land & Building	45,150
B	29,850		Goodwill	5,250
C	14,550	79,800		
		1,15,500		1,15,500

They agreed to take *D* into partnership and give him 1/8th share on the following terms :—

(1) That Furniture be depreciated by ₹2,920.

(2) An Old Customer, whose account was written off as bad, has promised to pay ₹2,000 in full settlement of his full debt.

(3) That a provision of ₹1,320 be made for outstanding repair bills.

(4) That the value of land and building having appreciated be brought upto ₹56,910.

(5) That *D* should bring in ₹14,700 as his capital.

(6) That *D* should bring in ₹14,070 as his share of goodwill.

(7) That after making the above adjustments, the capital accounts of old partners be adjusted on the basis of the proportion of *D*'s Capital to his share in business *i.e.*, actual cash to be paid off or brought in by the old partners, as the case may be.

Pass the necessary journal entries and prepare the balance sheet of the new firm.

SOLUTION:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	General Reserve A/c	Dr.		10,500	
	To *A*'s Capital A/c				4,500
	To *B*'s Capital A/c				3,750
	To *C*'s Capital A/c				2,250
	(General reserve transferred to old partners' capital accounts)				
	Revaluation A/c	Dr.		4,240	
	To Furniture A/c				2,920
	To Provision for Repairs A/c				1,320
	(Reduction in the value of assets and a provision made for outstanding repairs bills)				
	Debtors A/c*	Dr.		2,000	
	Land & Building A/c	Dr.		11,760	
	To Revaluation A/c				13,760
	(Increase in the value of assets)				
	Revaluation A/c	Dr.		9,520	
	To *A*'s Capital A/c				4,080
	To *B*'s Capital A/c				3,400
	To *C*'s Capital A/c				2,040
	(Transfer of profit on revaluation to old partner's Capital A/cs)				
	A's Capital A/c	Dr.		2,250	
	B's Capital A/c	Dr.		1,875	
	C's Capital A/c	Dr.		1,125	
	To Goodwill A/c				5,250
	(Goodwill appearing in the books written off)				
	Cash A/c	Dr.		28,770	
	To *D*'s Capital A/c				14,700
	To Premium for Goodwill A/c				14,070
	(Amount brought in cash by *D* being ₹14,700 for capital and ₹14,070 for goodwill)				
	Premium for Goodwill A/c	Dr.		14,070	
	To *A*'s Capital A/c				6,030
	To *B*'s Capital A/c				5,025
	To *C*'s Capital A/c				3,015
	(Goodwill brought in by *D* credited to old partners)				
	A's Capital A/c[1]	Dr.		3,660	
	B's Capital A/c[2]	Dr.		3,400	
	To Cash A/c				7,060
	(Cash withdrawn by *A* and *B*)				
	Cash A/c[3]	Dr.		1,320	
	To *C*'s Capital A/c				1,320
	(Cash brought in by *C*)				

* An old customer has acknowledged to pay ₹2,000 in full settlement of his debt. In this edition of the book, it has been included in Debtors because the amount is most likely to be received.

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	Particulars	₹
To Furniture A/c		2,920	By Land & Buildings A/c	11,760
To Provision for Repairs		1,320	By Debtors A/c	2,000
To Profit transferred to :				
A's Capital A/c	4,080			
B's Capital A/c	3,400			
C's Capital A/c	2,040	9,520		
		13,760		13,760

Dr. CAPITAL ACCOUNTS Cr.

Particulars	A	B	C	D	Particulars	A	B	C	D
	₹	₹	₹	₹		₹	₹	₹	₹
To Goodwill A/c	2,250	1,875	1,125		By Balance b/d	35,400	29,850	14,550	—
To Balance c/d	47,760	40,150	20,730	14,700	By General Reserve A/c	4,500	3,750	2,250	—
					By Revaluation A/c	4,080	3,400	2,040	—
					By Premium for Goodwill A/c	6,030	5,025	3,015	—
					By Cash A/c	—	—	—	14,700
	50,010	42,025	21,855	14,700		50,010	42,025	21,855	14,700
To Cash A/c (Balancing figure)	3,660	3,400	—	—	By Balance b/d	47,760	40,150	20,730	14,700
To Balance c/d	44,100	36,750	22,050	14,700	By Cash A/c (Balancing figure)	—	—	1,320	—
	47,760	40,150	22,050	14,700		47,760	40,150	22,050	14,700

BALANCE SHEET

As at ....

Liabilities		₹	Assets	₹
Creditors		18,900	Cash[4]	24,920
Bills Payable		6,300	Debtors	28,460
Provision for Repairs		1,320	Stock	29,400
Capital Accounts :—			Furniture	4,430
A	44,100		Land & Buildings	56,910
B	36,750			
C	22,050			
D	14,700	1,17,600		
		1,44,120		1,44,120

New profit sharing ratio will be calculated as under :

Share given to D $= \frac{1}{8}$

Balance of profits $= 1 - \frac{1}{8} = \frac{7}{8}$

A's new share $= \frac{7}{8} \times \frac{6}{14} = \frac{3}{8}$

B's new share $= \frac{7}{8} \times \frac{5}{14} = \frac{5}{16}$

C's new share $= \frac{7}{8} \times \frac{3}{14} = \frac{3}{16}$

D's share $= \frac{1}{8}$

$A : B : C : D = \frac{3}{8} : \frac{5}{16} : \frac{3}{16} : \frac{1}{8} = \frac{6}{16} : \frac{5}{16} : \frac{3}{16} : \frac{2}{16}$

D brings in ₹14,700 as Capital according to his 1/8th share of profit. Therefore, according to D's Capital, the total Capital of the new firm will be

$$= 14{,}700 \times \frac{8}{1} = ₹\ 1{,}17{,}600$$

$\therefore$ A's Capital in new firm $= 1{,}17{,}600 \times \frac{6}{16} =$ ₹44,100

B's Capital in new firm $= 1{,}17{,}600 \times \frac{5}{16} =$ ₹36,750

C's Capital in new firm $= 1{,}17{,}600 \times \frac{3}{16} =$ ₹22,050

D's Capital in new firm $= 1{,}17{,}600 \times \frac{2}{16} =$ ₹14,700

Notes :

1. A's Capital in the new firm should be ₹44,100, whereas his existing capital shown by his Capital A/c is ₹47,760. Therefore, his excess Capital ₹47,760 – ₹44,100 = 3,660 will be refunded to him.
2. B's Capital in the new firm should be ₹36,750, whereas his existing capital shown by his Capital A/c is ₹40,150. Therefore, his excess Capital ₹40,150 – ₹36,750 = ₹3,400 will be refunded to him.
3. C's Capital in the new firm should be ₹22,050, whereas his existing capital is only ₹20,730. Therefore, he will bring in ₹22,050 – 20,730 = ₹1,320.
4. Calculation of Cash Balance :

		₹
Opening Balance		1,890
Add : Capital and goodwill brought in by D		28,770
Add : Cash brought in by C		1,320
		31,980
Less : Amount paid to A	3,660	
Less : Amount paid to B	3,400	7,060
Closing Balance		24,920

ILLUSTRATION 77.

A, B and C are partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1.

D is admitted as a new partner for 1/4 share in the profits of the firm, which he gets 1/8 from A, and 1/16 each from B and C. The total capital of the new firm after D's admission will be ₹2,40,000. D is required to bring in cash equal to 1/4 of the total capital of the new firm. The capitals of the old partners also have to be adjusted in proportion of their profit sharing ratio. The capitals of A, B and C after all adjustments in respect of goodwill and revaluation of assets and liabilities have been made are A ₹80,000, B ₹30,000 and C ₹28,000. Calculate the capitals of all the partners and record the necessary journal entries for doing adjustments in respect of capitals according to the agreement between the partners.

SOLUTION :

D's share is $\frac{1}{4}$ which he acquires $\frac{1}{8}$ from A, $\frac{1}{16}$ from B and $\frac{1}{16}$ from C.

$$\therefore \quad A\text{'s new share} = \frac{3}{6} - \frac{1}{8} = \frac{24-6}{48} = \frac{18}{48}$$

$$B\text{'s new share} = \frac{2}{6} - \frac{1}{16} = \frac{16-3}{48} = \frac{13}{48}$$

$$C\text{'s new share} = \frac{1}{6} - \frac{1}{16} = \frac{8-3}{48} = \frac{5}{48}$$

$$D\text{'s share} = \frac{1}{4}$$

Thus, new profit sharing ratio between A, B, C and D is $\frac{18}{48} : \frac{13}{48} : \frac{5}{48} : \frac{1}{4}$

or $\frac{18 : 13 : 5 : 12}{48}$ or 18 : 13 : 5 : 12

Total Capital of the new firm will be ₹2,40,000

A's Capital in the new firm should be $= 2{,}40{,}000 \times \frac{18}{48}$ = ₹90,000

B's Capital in the new firm should be $= 2{,}40{,}000 \times \frac{13}{48}$ = ₹65,000

C's Capital in the new firm should be $= 2{,}40{,}000 \times \frac{5}{48}$ = ₹25,000

D's Capital in the new firm should be $= 2{,}40{,}000 \times \frac{12}{48}$ = ₹60,000

Hence, A will bring in ₹90,000 – ₹80,000 = ₹10,000
B will bring in ₹65,000 – ₹30,000 = ₹35,000
C will withdraw ₹28,000 – ₹25,000 = ₹ 3,000
D will bring in ₹60,000

Books of A, B, C and D

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.		45,000	
	To A's Capital A/c				10,000
	To B's Capital A/c				35,000
	(Deficit capital brought in by A and B)				

	C's Capital A/c Dr. To Bank A/c (Excess capital withdrawn by *C*)		3,000	3,000
	Bank A/c Dr. To *D*'s Capital A/c (Amount brought in by *D* as capital)		60,000	60,000

ILLUSTRATION 78.

Hari and Kavi are partners sharing profits and losses in the ratio of 3 : 2. They admit Ravi as a partner who contributes ₹30,000 as his capital for 1/5th share in the profits of the firm. It is decided that after Ravi's admission, the capitals of the Hari and Kavi will be adjusted on the basis of Ravi's share of capital in the business, any surplus or deficiency to be adjusted through current accounts. Before any adjustments were made, the capitals of Hari and Kavi were : ₹59,000 and ₹35,000 respectively.

At the time of Ravi's admission :

(*a*) The firm's goodwill was valued at ₹40,000.

(*b*) General Reserve was ₹25,000.

(*c*) Loss on revaluation of assets and liabilities was ₹4,000.

You are required to pass the necessary journal entries on Ravi's admission.

(ISC Specimen Question Paper, 2018)

SOLUTION : JOURNAL

Date	*Particulars*	*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Ravi's Current A/c (1/5th of 40,000) Dr. To Hari's Capital A/c (3/5 of 8,000) To Kavi's Capital A/c (2/5 of 8,000) (Adjustment for Goodwill in sacrificing ratio)		8,000	 4,800 3,200
	General Reserve A/c Dr. To Hari's Capital A/c To Kavi's Capital A/c (Transfer of general reserve to old partners)		25,000	 15,000 10,000
	Hari's Capital A/c Dr. Kavi's Capital A/c Dr. To Revaluation A/c (Transfer of loss on revaluation)		2,400 1,600	 4,000
	Bank A/c Dr. To Ravi's Capital A/c (Amount brought in by Ravi as capital)		30,000	 30,000
	Hari's Capital A/c Dr. To Hari's Current A/c (Surplus Capital Credited to Hari's Current A/c)		4,400	 4,400
	Kavi's Current A/c Dr. To Kavi's Capital A/c (Deficit capital debited to Kavi's Current A/c)		1,400	 1,400

Working Notes :

(*i*) Hari's Capital = 59,000 + 4,800 + 15,000 – 2,400 = ₹76,400

Kavi's Capital = 35,000 + 3,200 + 10,000 – 1,600 = ₹46,600

(*ii*) New Profit Sharing Ratios :

Ravi's Share = $\frac{1}{5}$; Remaining Share = $1 - \frac{1}{5} = \frac{4}{5}$

Hari's New Share = $\frac{4}{5} \times \frac{3}{5} = \frac{12}{25}$

Kavi's New Share = $\frac{4}{5} \times \frac{2}{5} = \frac{8}{25}$

Ravi's Share = $\frac{1}{5}$ or $\frac{5}{25}$

(*iii*) Ravi brings in ₹30,000 for his $\frac{1}{5}$th share. Hence, total capital of the new firm

= ₹30,000 × $\frac{5}{1}$ = ₹1,50,000

Hari's Capital in the new firm = 1,50,000 × $\frac{12}{25}$ = ₹72,000

Kavi's Capital in the new firm = 1,50,000 × $\frac{8}{25}$ = ₹48,000

	Hari (₹)	*Kavi* (₹)
Existing Capitals	76,400	46,600
Required Capitals in the new firm	72,000	48,000
Transferred to Current Accounts	4,400 Cr.	1,400 Dr.

ILLUSTRATION 79.

A, *B* and *C* are partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. Their Balance Sheet as at 31st March, 2022 is as follows :

Liabilities		₹	*Assets*		₹
Sundry Creditors		36,000	Cash		14,000
Bank Overdraft		20,000	Sundry Debtors	50,000	
Reserve		15,000	*Less* : Provision	2,500	47,500
Capital Accounts :			Stock		60,000
A	60,000		Patents		6,000
B	60,000		Fixed Assets		98,500
C	50,000	1,70,000	Goodwill		15,000
		2,41,000			2,41,000

On 1st April, 2022, *D* is admitted into the firm with 1/4th share in the profits, which he gets 1/8th from *A* and 1/8th from *B*. Other terms of agreement are as under :

(*a*) *D* will introduce ₹60,000 as his capital and pay ₹18,000 as his share of goodwill.

(*b*) 20% of the reserve is to remain as a provision against bad and doubtful debts.

(*c*) A liability to the extent of ₹1,000 be created in respect of a claim for damages against the firm.

(*d*) An item of ₹4,000 included in sundry creditors is not likely to be claimed.

(*e*) Stock is to be reduced by 30% and patents to be written off in full.

(*f*) *A* is to pay off the Bank Overdraft.

After making the above adjustments the capital accounts of the old partners be adjusted on the basis of *D*'s capital to his share in the business, *i.e.*, actual cash to be paid off to, or brought in by, the old partners, as the case may be.

Prepare journal entries, Capital Accounts and the Balance Sheet of the new firm.

SOLUTION :

JOURNAL ENTRIES

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2022					
April 1	Reserve A/c	Dr.		15,000	
	To Provision for Doubtful Debts A/c				3,000
	To *A*'s Capital A/c				6,000
	To *B*'s Capital A/c				4,000
	To *C*'s Capital A/c				2,000
	(20% of Reserve retained as provision for doubtful debts and the balance credited to old partners in 3 : 2 : 1)				
	Revaluation A/c	Dr.		25,000	
	To Claim for Damages A/c				1,000
	To Stock A/c				18,000
	To Patents A/c				6,000
	(Recording the liability for damages and decrease in the value of stock and patents)				
	Sundry Creditors A/c	Dr.		4,000	
	To Revaluation A/c				4,000
	(Decrease in the creditors)				
	A's Capital A/c	Dr.		10,500	
	B's Capital A/c	Dr.		7,000	
	C's Capital A/c	Dr.		3,500	
	To Revaluation A/c				21,000
	(Transfer of loss on revaluation)				
	Bank Overdraft A/c	Dr.		20,000	
	To *A*'s Capital A/c				20,000
	(Bank Overdraft paid off by *A* credited to his capital A/c)				
	A's Capital A/c	Dr.		7,500	
	B's Capital A/c	Dr.		5,000	
	C's Capital A/c	Dr.		2,500	
	To Goodwill A/c				15,000
	(Goodwill already existing in the books written off in the old ratio)				

Cash A/c Dr.		78,000	
To *D*'s Capital A/c			60,000
To Premium for Goodwill A/c			18,000
(*D* brings in ₹60,000 for his capital and ₹18,000 as his share of goodwill)			
Premium for Goodwill A/c Dr.		18,000	
To *A*'s Capital A/c			9,000
To *B*'s Capital A/c			9,000
(Amount of goodwill shared by *A* and *B* in their sacrificing ratio *i.e.* 1 : 1)			
Cash A/c Dr.		13,000	
To *A*'s Capital A/c			13,000
(Deficit capital brought in by *A*)			
B's Capital A/c Dr.		11,000	
C's Capital A/c Dr.		6,000	
To Cash A/c			17,000
(Surplus capital withdrawn by *B* and *C*)			

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*D*	*Particulars*	*A*	*B*	*C*	*D*
	₹	₹	₹	₹		₹	₹	₹	₹
To Rev.	10,500	7,000	3,500	—	By Bal. b/d	60,000	60,000	50,000	—
To Good-will	7,500	5,000	2,500	—	By Reserve	6,000	4,000	2,000	—
To Bal. c/d	77,000	61,000	46,000	60,000	By Bank Overdraft	20,000	—	—	—
					By Cash				60,000
					By Premium for Goodwill A/c	9,000	9,000	—	—
	95,000	73,000	52,000	60,000		95,000	73,000	52,000	60,000
To Cash	—	11,000	6,000	—	By Bal. b/d	77,000	61,000	46,000	60,000
To Bal. c/d	90,000	50,000	40,000	60,000	By Cash	13,000			
	90,000	61,000	46,000	60,000		90,000	61,000	46,000	60,000

BALANCE SHEET *as at 1st April, 2022*

Liabilities	₹	*Assets*		₹
Sundry Creditors	32,000	Cash		88,000
Claim for Damages	1,000	Sundry Debtors	50,000	
Capital Accounts :		*Less* : Provision	5,500	44,500
A	90,000	Stock		42,000
B	50,000	Fixed Assets		98,500
C	40,000			
D	60,000			
	2,73,000			2,73,000

Working Notes : (1) New Profit sharing ratios :

$A = \frac{3}{6} - \frac{1}{8} = \frac{3}{8}$

$B = \frac{2}{6} - \frac{1}{8} = \frac{5}{24}$

$C = \frac{1}{6}$

$D = \frac{1}{4}$

Hence, the new profit sharing ratio between A, B, C and D will be : $\frac{3}{8} : \frac{5}{24} : \frac{1}{6} : \frac{1}{4}$

or $\frac{9}{24} : \frac{5}{24} : \frac{4}{24} : \frac{6}{24}$ or 9 : 5 : 4 : 6

D brings in ₹60,000 as his capital according to his 1/4th share of profit. Therefore, based on D's capital, the total capital of the new firm will be $60{,}000 \times \frac{4}{1}$ = ₹2,40,000

∴ A's Capital in the new firm = $2{,}40{,}000 \times \frac{9}{24}$ = ₹90,000

B's Capital in the new firm = $2{,}40{,}000 \times \frac{5}{24}$ = ₹50,000

C's Capital in the new firm = $2{,}40{,}000 \times \frac{4}{24}$ = ₹40,000

D's Capital in the new firm = $2{,}40{,}000 \times \frac{6}{24}$ = ₹60,000

Hence, A will bring in ₹90,000 – ₹77,000 = ₹13,000
B will withdraw ₹61,000 – ₹50,000 = ₹11,000
C will withdraw ₹46,000 – ₹40,000 = ₹ 6,000

(2) Cash Balance = ₹14,000 + ₹78,000 + ₹13,000 – ₹11,000 – ₹6,000 = ₹88,000

ILLUSTRATION 80.

X and Y share profits in the ratio of 3 : 1. Their Balance Sheet as at 31st March, 2022, was as under :

Liabilities	₹	*Assets*	₹
Outstanding Expenses	5,000	Cash	7,800
Sundry Creditors	36,000	Sundry Debtors	24,000
Provision for Doubtful Debts	800	Stock	5,000
Capital Accounts :		Fixed Assets	80,000
X	68,000	Goodwill	8,000
Y	31,000	P & L A/c	16,000
	1,40,800		1,40,800

Z is admitted into partnership on 1st April, 2022 the following terms :—

(*i*) Fixed assets are overvalued by 25%.

(*ii*) Provision for doubtful debts should remain at 5% on debtors.

(*iii*) The new profit sharing ratio will be 5 : 3 : 2.

(*iv*) *Z* will pay ₹20,000 as capital and the capitals of old partners will be adjusted on the basis of new partner's capital and his share in the business, actual cash to be brought in or withdrawn by old partners, as the case may be.

(*v*) Goodwill of the firm is valued at ₹20,000.

Prepare journal entries, capital accounts and the opening Balance Sheet of the new firm.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2022					
April 1	*X*'s Capital A/c	Dr.		12,000	
	Y's Capital A/c	Dr.		4,000	
	To P & L A/c				16,000
	(Transfer of debit balance of P & L A/c)				
	Revaluation A/c	Dr.		16,400	
	To Fixed Assets A/c(1)				16,000
	To Provision for Doubtful Debts A/c				400
	(Decrease in the value of fixed assets and increase required in provision for doubtful debts)				
	X's Capital A/c	Dr.		12,300	
	Y's Capital A/c	Dr.		4,100	
	To Revaluation A/c				16,400
	(Loss on revaluation transferred to old partners)				
	X's Capital A/c	Dr.		6,000	
	Y's Capital A/c	Dr.		2,000	
	To Goodwill A/c				8,000
	(Goodwill already appearing in the books written off in old profit sharing ratio *i.e.*, 3 : 1)				
	Y's Capital A/c(1) (1/20 of 20,000)	Dr.		1,000	
	Z's Current A/c(2) (4/20 of 20,000)	Dr.		4,000	
	To *X*'s Capital A/c (5/20 of 20,000)				5,000
	(*X* compensated for goodwill due to his sacrificing 5/20th share, *Y* gaining 1/20th and *Z* gaining 4/20th share)				
	Cash A/c	Dr.		20,000	
	To *Z*'s Capital A/c				20,000
	(Capital introduced by *Z*)				
	Cash A/c	Dr.		17,400	
	To *X*'s Capital A/c				7,300
	To *Y*'s Capital A/c				10,100
	(Deficit capital brought in by *X* and *Y*)				

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*X*	*Y*	*Z*	*Particulars*	*X*	*Y*	*Z*
	₹	₹	₹		₹	₹	₹
To P & L A/c	12,000	4,000		By Bal. b/d	68,000	31,000	—

	X	Y	Z		X	Y	Z
To Revaluation	12,300	4,100	—	By Y's Capital A/c	1,000		
To Goodwill	6,000	2,000		By Z's Current A/c	4,000		
To X's Capital A/c		1,000		By Cash			20,000
To Bal. c/d	42,700	19,900	20,000				
	73,000	31,000	20,000		73,000	31,000	20,000
				By Bal. b/d	42,700	19,900	20,000
To Bal. c/d	50,000	30,000	20,000	By Cash	7,300	10,100	
	50,000	30,000	20,000		50,000	30,000	20,000

BALANCE SHEET *as at 1st April, 2022*

Liabilities		₹	*Assets*		₹
Outstanding Expenses		5,000	Cash		45,200
Sundry Creditors		36,000	Sundry Debtors	24,000	
Capital Accounts :			*Less* : Provision	1,200	22,800
X	50,000		Stock		5,000
Y	30,000		Fixed Assets		64,000
Z	20,000	1,00,000	*Z*'s Current A/c		4,000
		1,41,000			1,41,000

Working Notes :

(1) Actual Value of Fixed Assets : $80,000 \times \frac{100}{125} = ₹64,000$

(2) Calculation of Sacrificing and Gaining Ratio :

Old Ratio of *X* and *Y* $= \frac{3}{4} : \frac{1}{4}$

New Ratio of *X, Y* and *Z* $= \frac{5}{10} : \frac{3}{10} : \frac{2}{10}$

X $= \frac{3}{4} - \frac{5}{10} = \frac{15 - 10}{20} = \frac{5}{20}$ (Sacrifice)

Y $= \frac{1}{4} - \frac{3}{10} = \frac{5 - 6}{20} = \frac{1}{20}$ (Gain)

Z $= \frac{2}{10}$ or $\frac{4}{20}$ (Gain)

(3) The profit sharing ratio is 5 : 3 : 2. Therefore, based on *Z*'s capital, the total capital of the new firm will be $20,000 \times \frac{10}{2} = ₹1,00,000$.

∴ *X*'s Capital in the new firm $= 1,00,000 \times \frac{5}{10} = ₹50,000$

Y's Capital in the new firm $= 1,00,000 \times \frac{3}{10} = ₹30,000$

Z's Capital in the new firm $= 1,00,000 \times \frac{2}{10} = ₹20,000$

Hence, *X* will bring in ₹50,000 – ₹42,700 = ₹ 7,300
Y will bring in ₹30,000 – ₹19,900 = ₹10,100

(4) Cash balance = ₹7,800 + ₹20,000 + ₹7,300 + ₹10,100 = ₹45,200.

ILLUSTRATION 81.

Anil and Sunil are partners sharing profits and losses in the ratio of 3 : 2. They admit Charan as a new partner from 1st April, 2013. Anil gives 1/3rd of his share while Sunil gives 1/10th from his share to Charan. Their Balance Sheet as on 31st March, 2013, is given below :

Liabilities	₹	*Assets*	₹
Anil's Capital	32,600	Land & Building	6,000
Sunil's Capital	40,400	Investments	
Workmen Compensation Fund	2,000	(Market Value ₹4,500)	5,000
Investment Fluctuation Fund	1,000	Debtors	30,000
Employee's Provident Fund	1,000	Stock	10,000
Provision for Doubtful Debts	1,000	Bank	27,000
	78,000		78,000

Terms of Charan's admission are as follows :

(*a*) Charan brings in ₹30,000 as his capital. His share of Goodwill was determined to be ₹18,000. He could bring in only 60% of his share.

(*b*) Land & Building was found to be undervalued by ₹10,000, stock was found overvalued by ₹7,000 and provision for doubtful debts is to be made equal to 5% of the debtors.

(*c*) Capital accounts of the old partners to be re-adjusted in the new profit sharing arrangement on the basis of Charan's capital, any excess or deficiency to be adjusted in cash.

You are required to :

(*i*) Pass journal entries

(*ii*) Prepare Partner's Capital Accounts

(*iii*) Balance Sheet of the new firm.

Show your workings clearly. *(I.S.C. Sample Question paper 2015)*

SOLUTION : JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2013					
April 1	Investment Fluctuation Fund A/c	Dr.		500	
	To Investments A/c				500
	(Value of Investments brought down to market value)				
April 1	Investment Fluctuation Fund A/c	Dr.		500	
	Workmen Compensation Fund A/c	Dr.		2,000	
	To Anil's Capital A/c				1,500
	To Sunil's Capital A/c				1,000
	(Transfer of accumulated profits to old partner's Capital Accounts)				

April 1	Land & Building A/c	Dr.	10,000	
	To Revaluation A/c			10,000
	(Increase in the value of Land & Building)			
April 1	Revaluation A/c	Dr.	7,500	
	To Stock A/c			7,000
	To Provision for Doubtful Debts A/c			500
	(Decrease in the value of assets)			
April 1	Revaluation A/c	Dr.	2,500	
	To Anil's Capital A/c			1,500
	To Sunil's Capital A/c			1,000
	(Transfer of profit on revaluation)			
April 1	Bank A/c	Dr.	40,800	
	To Charan's Capital A/c			30,000
	To Premium for Goodwill A/c			10,800
	(Amount brought in by Charan as his Capital and 60% part of his share of goodwill)			
April 1	Premium for Goodwill A/c	Dr.	10,800	
	Charan's Current A/c	Dr.	7,200	
	To Anil's Capital A/c			12,000
	To Sunil's Capital A/c			6,000
	(Premium for goodwill credited to old partners in their sacrificing ratio *i.e.*, 2 : 1)			
April 1	Anil's Capital A/c	Dr.	7,600	
	Sunil's Capital A/c	Dr.	18,400	
	To Bank A/c			26,000
	(Surplus Capital withdrawn by Anil and Sunil)			

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*Anil*	*Sunil*	*Charan*	*Particulars*	*Anil*	*Sunil*	*Charan*
	₹	₹	₹		₹	₹	₹
To Bal. c/d	47,600	48,400	30,000	By Bal. b/d	32,600	40,400	
				By Sundries (Accumulated profits)	1,500	1,000	
				By Revaluation A/c	1,500	1,000	
				By Bank A/c			30,000
				By Premium for Goodwill	7,200	3,600	
				By Charan's Current A/c	4,800	2,400	
	47,600	48,400	30,000		47,600	48,400	30,000
To Bank A/c	7,600	18,400		By Bal. b/d	47,600	48,400	30,000
To Bal. c/d	40,000	30,000	30,000				
	47,600	48,400	30,000		47,600	48,400	30,000

BALANCE SHEET

as at 1st April, 2013

Liabilities		₹	*Assets*	₹
Capital Accounts :			Land & Building	16,000
Anil	40,000		Investments (Market Value)	4,500
Sunil	30,000		Debtors	30,000
Charan	30,000	1,00,000	Stock	3,000
Employee's Provident Fund		1,000	Bank (₹27,000 + ₹40,800	
Provision for Doubtful Debts		1,500	– ₹7,600 – ₹18,400)	41,800
			Charan's Current A/c	7,200
		1,02,500		1,02,500

Working Notes :

(1) Calculation of Sacrificing Ratios :

(*i*) Anil's old share $= \frac{3}{5}$; He surrenders $\frac{1}{3}$ of his share

Hence, share surrendered by Anil $= \frac{3}{5} \times \frac{1}{3} = \frac{1}{5}$

(*ii*) Sunil's old share $= \frac{2}{5}$; He surrenders $\frac{1}{10}$ from his share

Hence, share surrendered by Sunil $= \frac{1}{10}$

Sacrifice Ratio $= \frac{1}{5} : \frac{1}{10}$ or 2 : 1

(2) Calculation of New Ratios :

Anil $= \frac{3}{5} - \frac{1}{5} = \frac{2}{5}$

Sunil $= \frac{2}{5} - \frac{1}{10} = \frac{4-1}{10} = \frac{3}{10}$

Charan $= \frac{1}{5} + \frac{1}{10} = \frac{2+1}{10} = \frac{3}{10}$

Hence, New ratio of Anil, Sunil and Charan $= \frac{2}{5} : \frac{3}{10} : \frac{3}{10}$ or 4 : 3 : 3

(3) Based on Charan's Capital, the total Capital of the new firm should be :

$₹30{,}000 \times \frac{10}{3} = ₹\ 1{,}00{,}000$

∴ Anil's Capital in the new firm $= 1{,}00{,}000 \times \frac{4}{10} = ₹\ 40{,}000$

Sunil's Capital in the new firm $= 1{,}00{,}000 \times \frac{3}{10} = ₹\ 30{,}000$

Hence, Anil will withdraw ₹47,600 – ₹40,000 = ₹ 7,600

Sunil will withdraw ₹48,400 – ₹30,000 = ₹18,400

ILLUSTRATION 82.

A and *B* are partners in a firm sharing profits and losses in the ratio of 2 : 1. Their Balance Sheet as at 31.3.2022 stood as follows :

Liabilities	₹	*Assets*	₹
Sundry Creditors	80,000	Land and Buildings	2,00,000
General Reserve	60,000	Stock	1,10,000
Provision for Repairing of building	20,000	Sundry Debtors	1,50,000
Capitals :		Bank	20,000
A	2,20,000		
B	1,00,000		
	4,80,000		4,80,000

On 1st April 2022, they admit *C* as a partner and the following terms were agreed upon :

(*i*) The new profit sharing ratio should be 2 : 1 : 1.

(*ii*) *C* is to bring in ₹1,30,000 as his capital.

(*iii*) Goodwill is to be valued on the basis of Capitalisation at 12% of the normal average profits of the last three years. Profits of the last three years were as follows :
For the year ended 31.3.2020 profit ₹15,000 (including insurance claim received ₹50,000).
For the year ended 31.3.2021 loss ₹20,000 (including voluntary retirement compensation paid ₹1,00,000).
For the year ended 31.3.2022 profit ₹1,75,000 (including a profit of ₹40,000 on the sale of assets).

(*iv*) *C* is to bring half of his share of goodwill in cash and the other half was to be purchased by him from *A* and *B* which is to be debited to *C*'s Current Account.

(*v*) Of the sundry debtors, ₹15,000 proved to be bad and there is doubtful amount of ₹7,000.

(*vi*) Provision is to be made for an unrecorded bill of a supplier amounting to ₹20,000. Provision for repair of building should also be increased by ₹10,000.

(*vii*) Land and Buildings are to be increased to ₹2,40,000.

(*viii*) Capitals to be adjusted according to profit sharing ratio taking *C*'s capital as the base, any excess or shortfall to be adjusted in cash.

Show necessary journal entries and draw up the readjusted balance sheet of the new firm.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2022					
April 1	General Reserve A/c	Dr.		60,000	
	To *A*'s Capital A/c				40,000
	To *B*'s Capital A/c				20,000
	(Transfer of general reserve to old partners)				

Revaluation A/c	Dr.	52,000	
To Sundry Debtors A/c			15,000
To Provision for Doubtful Debts A/c			7,000
To Sundry Creditors A/c			20,000
To Provision for Repairing of Building A/c			10,000
(Recording of decrease in debtors and increase in liabilities)			
Land and Buildings A/c	Dr.	40,000	
To Revaluation A/c			40,000
(Recording of increase in the value of land and buildings)			
A's Capital A/c	Dr.	8,000	
B's Capital A/c	Dr.	4,000	
To Revaluation A/c			12,000
(Loss on revaluation transferred to old partner's capital accounts)			
Bank A/c	Dr.	1,45,000	
To *C*'s Capital A/c			1,30,000
To Premium for Goodwill A/c(1)			15,000
(Amount brought in by *C* as his capital and half of his share of goodwill)			
Premium for Goodwill A/c	Dr.	15,000	
C's Current A/c	Dr.	15,000	
To *A*'s Capital A/c			20,000
To *B*'s Capital A/c			10,000
(Premium for goodwill credited to old partners in sacrificing ratio *i.e.* 2 : 1)			
A's Capital A/c	Dr.	12,000	
To Bank A/c			12,000
(Excess capital withdrawn by *A*)			
Bank A/c	Dr.	4,000	
To *B*'s Capital A/c			4,000
(Deficit capital brought in by *B*)			

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Revaluation A/c	8,000	4,000	—	By Bal. b/d	2,20,000	1,00,000	—
To Bal. c/d	2,72,000	1,26,000	1,30,000	By General Res.	40,000	20,000	—
				By Bank			1,30,000
				By Sundries (Premium for goodwill)	20,000	10,000	—
	2,80,000	1,30,000	1,30,000		2,80,000	1,30,000	1,30,000
To Bank A/c	12,000	—	—	By Bal. b/d	2,72,000	1,26,000	1,30,000
To Bal. c/d	2,60,000	1,30,000	1,30,000	By Bank A/c	—	4,000	—
	2,72,000	1,30,000	1,30,000		2,72,000	1,30,000	1,30,000

BALANCE SHEET *as at 1st April, 2022*

Liabilities	₹	*Assets*		₹
Sundry Creditors	1,00,000	Land and Buildings		2,40,000
Provision for Repairing of Building	30,000	Stock		1,10,000
Capital Accounts :		Sundry Debtors		
A	2,60,000	(1,50,000 – 15,000)	1,35,000	
B	1,30,000	*Less* : Provision for		
C	1,30,000	Doubtful debts	7,000	1,28,000
		Bank		1,57,000
		C's Current Account		15,000
	6,50,000			6,50,000

Working Note :

(1) Valuation of Goodwill :

	₹	₹
Profit for the year ended 31.3.2020	15,000	
Less : Insurance Claim	50,000	(–) 35,000
Profit/Loss for the year ended 31.3.2021	(–) 20,000	
Add : Voluntary retirement compensation	1,00,000	(+) 80,000
Profit for the year ended 31.3.2022	1,75,000	
Less : Profit on sale of assets	40,000	(+) 1,35,000
		1,80,000

Average Profit = 1,80,000 ÷ 3 = ₹60,000

Capitalised value of Average Profit $= \text{Average Profit} \times \frac{100}{\text{Normal Rate of Return}}$

$= 60,000 \times \frac{100}{12} = ₹5,00,000$

	A	*B*
Capital Employed	2,20,000	1,00,000
(+) General Reserve of ₹60,000 distributed in the ratio of 2 : 1	40,000	20,000
	2,60,000	1,20,000

2,60,000 + 1,20,000 = 3,80,000

Goodwill= Capitalised value of Average Profits – Capital Employed

= 5,00,000 – 3,80,000 = 1,20,000

Premium for Goodwill payable by $C = 1,20,000 \times \frac{1}{4} = ₹30,000$. Half of ₹30,000 has been brought in by *C* in cash and the other half has been debited to his current account.

(2) On the basis of *C*'s share, the total capital of the new firm should be

$₹1,30,000 \times \frac{4}{1} = ₹5,20,000.$

∴ *A*'s Capital in the new firm should be $= 5,20,000 \times \frac{2}{4} = ₹2,60,000$

B's Capital in the new firm should be $= 5,20,000 \times \frac{1}{4} = ₹1,30,000$

Hence, *A* will withdraw ₹2,72,000 – ₹2,60,000 = ₹12,000
B will bring in ₹1,30,000 – ₹1,26,000 = ₹ 4,000

(3) Bank Balance = ₹20,000 + ₹1,45,000 – ₹12,000 + ₹4,000 = ₹1,57,000

ILLUSTRATION 83.

Badal and Bijli were partners in a firm sharing profits in the ratio of 3 : 2. Their Balance Sheet as at 31st March, 2019 was as follows :

BALANCE SHEET OF BADAL AND BIJLI
as at 31st March, 2019

Liabilities		*Amount*	*Assets*	*Amount*
		₹		₹
Capitals :			Building	1,50,000
Badal	1,50,000		Investments	73,000
Bijli	90,000	2,40,000	Stock	43,000
Badal's Current A/c		12,000	Debtors	20,000
Investment Fluctuation Reserve		24,000	Cash	22,000
Bills Payable		8,000	Bijli's Current A/c	2,000
Creditors		26,000		
		3,10,000		3,10,000

Raina was admitted on the above date as a new partner for $\frac{1}{6}$th share in the profits of the firm. The terms of agreement were as follows :

(*i*) Raina will bring ₹40,000 as her capital and capitals of Badal and Bijli will be adjusted on the basis of Raina's capital by opening current accounts.

(*ii*) Raina will bring her share of goodwill premium for ₹12,000 in cash.

(*iii*) The building was overvalued by ₹15,000 and stock by ₹3,000.

(*iv*) A provision of 10% was to be created on debtors for bad debts.

Prepare the Revaluation Account and Current and Capital Accounts of Badal, Bijli and Raina. *(C.B.S.E. 2020, Chennai, Mumbai)*

SOLUTION :

Dr. REVALUATION A/C Cr.

Particulars	*Amount*	*Particulars*		*Amount*
	₹			₹
To Building A/c	15,000	By Loss on Revaluation tfd. to :		
To Stock A/c	3,000	Badal's Current A/c	12,000	
To Provision for Bad Debts A/c	2,000	Bijli's Current A/c	8,000	20,000
	20,000			20,000

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*Badal*	*Bijli*	*Raina*	*Particulars*	*Badal*	*Bijli*	*Raina*
	₹	₹	₹		₹	₹	₹
To Badal's Current A/c	30,000	—	—	By Balance b/d	1,50,000	90,000	—
				By Bank A/c	—	—	40,000

To Bijli's Current A/c	—	10,000	—				
To Balance c/d	1,20,000	80,000	40,000				
	1,50,000	90,000	40,000		1,50,000	90,000	40,000

Dr. PARTNER'S CURRENT ACCOUNTS Cr.

Particulars	*Badal*	*Bijli*	*Particulars*	*Badal*	*Bijli*
	₹	₹		₹	₹
To Balance b/d	—	2,000	By Balance b/d	12,000	—
To Revaluation A/c	12,000	8,000	By Premium for Goodwill A/c	7,200	4,800
To Balance c/d	51,600	14,400	By Investment Fluctuation Reserve	14,400	9,600
			By Badal's Capital A/c	30,000	—
			By Bijli's Capital A/c	—	10,000
	63,600	24,400		63,600	24,400

Working Note :

Raina's Share $= \frac{1}{6}$; Remaining Share $= 1 - \frac{1}{6} = \frac{5}{6}$

Badal's New Share $= \frac{3}{5}$ of $\frac{5}{6} = \frac{3}{6}$

Bijli's New Share $= \frac{2}{5}$ of $\frac{5}{6} = \frac{2}{6}$

Raina's Share $= \frac{1}{6}$

Raina's Capital is ₹40,000 and his share of profit is $\frac{1}{6}$

Hence, Total Capital of the firm will be : $40,000 \times \frac{6}{1}$ = ₹2,40,000

Badal's Capital in the new firm = $2,40,000 \times \frac{3}{6}$ = ₹1,20,000

Bijli's Capital in the new firm = $2,40,000 \times \frac{2}{6}$ = ₹ 80,000

	Badal (₹)	*Bijli* (₹)
Existing Capitals	1,50,000	90,000
Required Capitals	1,20,000	80,000
Transfer to Current Accounts	30,000 (Cr.)	10,000 (Cr.)

Accounting Treatment of Reserves and Accumulated Profits/Losses when old partners do not want to distribute them :

If, at the time of admission of a new partner, there are reserves and accumulated profits appearing in the Balance Sheet and the old partners decide to leave the reserves and accumulated profits undistributed, it will be necessary to pass an adjusting entry for the same. This is, because, at present only the old partners are entitled to share such reserves and profits in the old profit sharing ratio whereas in future all of them

including the new partner will be entitled to share such reserves and profits in the new profit sharing ratio. Hence, the new partner must compensate the sacrificing partners that share of reserves and profits which is proportionate to the share gained by him.

For example, suppose *A* and *B* sharing profits in the ratio of 3 : 2 decide to admit *C* as a new partner and decide to share future profits in equal proportion. Reserves appearing in the Balance Sheet amount to ₹60,000 and the partners do not want to distribute them. In such a case at present *A* is entitled to ₹36,000 and *B* ₹24,000 of such reserves but in future, after admitting *C* each would be entitled to ₹20,000. Hence, *C* must compensate *A* and *B* to the extent of ₹20,000 in the ratio of sacrifice made by them :

Sacrificing Ratio = Old Ratio – New Ratio

A Sacrifices : $\frac{3}{5} - \frac{1}{3} = \frac{9-5}{15} = \frac{4}{15}$

B Sacrifices : $\frac{2}{5} - \frac{1}{3} = \frac{6-5}{15} = \frac{1}{15}$

Thus, Sacrificing Ratio $= \frac{4}{15} : \frac{1}{15}$ or 4 : 1

The adjustment for this amount will be made by passing an adjustment entry wherein *C*'s Current A/c will be debited and Capital A/cs of *A* and *B* will be credited in their sacrificing ratio :

C's Current A/c	Dr.	20,000	
To *A*'s Capital A/c $(20,000 \times \frac{4}{5})$			16,000
To *B*'s Capital A/c $(20,000 \times \frac{1}{5})$			4,000
(Adjustment for Reseves on admission of *C*)			

ILLUSTRATION 84.

A and *B* are partners in a firm sharing profits in the ratio of 4 : 3. On March 31, 2022 their Balance Sheet showed a General Reserve of ₹35,000. On that date they decided to admit Sewak as a new partner and the new profit-sharing ratio will be 5 : 3 : 2. Record necessary journal entries in the books of the firm under the following circumstances :

(*i*) When they want to distribute the general reserve.

(*ii*) When they don't want to distribute the general reserve but prefer to record an adjustment entry for the same.

SOLUTION :

Case (*i*) When General Reserve is to be distributed :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022 March 31	General Reserve A/c	Dr.		35,000	
	To *A*'s Capital A/c $(35,000 \times \frac{4}{7})$				20,000

	To B's Capital A/c $(35,000 \times \frac{3}{7})$			15,000
	(General reserve transferred to the Capital accounts of old partners in their old ratio)			

Case (*ii*) When General Reserve is not to be distributed :

Old Ratio of A and B = 4 : 3

New Ratio of A, B and Sewak = 5 : 3 : 2

Sacrifice or Gain :

$$A = \frac{4}{7} - \frac{5}{10} = \frac{40-35}{70} = \frac{5}{70} \quad \text{(Sacrifice)}$$

$$B = \frac{3}{7} - \frac{3}{10} = \frac{30-21}{70} = \frac{9}{70} \quad \text{(Sacrifice)}$$

$$\text{Sewak} = \frac{2}{10} \text{ or } \frac{14}{70} \quad \text{(Gain)}$$

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2022 March 31	Sewak's Current A/c $(\frac{14}{70}$ of 35,000) Dr.		7,000	
	To A's Capital A/c $(\frac{5}{70}$ of 35,000)			2,500
	To B's Capital A/c $(\frac{9}{70}$ of 35,000)			4,500
	(Adjustment for general reserve on the admission of Sewak)			

ILLUSTRATION 85.

On 1st April, 2022, A, B and C sharing profits in the ratio of 3 : 2 : 1 admit D for $\frac{1}{6}$th share in profits. They maintain their accounts on fixed capital system. On this date their Balance Sheet disclosed the following items :

	₹
General Reserve	1,20,000
Profit & Loss (Cr. Balance)	60,000

Goodwill of the firm is valued at ₹90,000. However, D is unable to bring his share of goodwill in Cash.

Partners do not want to distribute the general reserve and profit but prefer to record the change in the profit sharing ratio by passing an adjustment entry. You are required to give the adjusting entry.

SOLUTION :

Adjustment to be made for :

	₹
General Reserve	1,20,000
Profit & Loss	60,000

Goodwill	90,000
	2,70,000

Since new profit sharing ratios are not given, old profit sharing ratio will be considered as sacrificing ratio.

Adjustment Entry : JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
April 1	D's Current A/c (2,70,000 × $\frac{1}{6}$)	Dr.		45,000	
	To A's Current A/c (45,000 × $\frac{3}{6}$)				22,500
	To B's Current A/c (45,000 × $\frac{2}{6}$)				15,000
	To C's Current A/c (45,000 × $\frac{1}{6}$)				7,500
	(Adjustment for accumulated profits and goodwill on the admission of C)				

ILLUSTRATION 86.

Mohan and Naresh are partners sharing profits and losses in the ratio of 3 : 2. Gopal is admitted into partnership. Mohan sacrifices $\frac{1}{3}$rd of his share and Naresh $\frac{1}{4}$th of his share in favour of Gopal. On this date, their Balance Sheet disclosed the following items :

BALANCE SHEET

as at .... *(Extracts)*

Liabilities	₹	*Assets*	₹
		Profit & Loss A/c (Dr. Bal.)	30,000
		Advertisement Suspense A/c	20,000

Partners do not want to distribute the accumulated losses but prefer to record the same by passing an adjustment entry. Pass the necessary journal entry.

SOLUTION :

Adjustment to be made for :

	₹
Dr. Balance of Profit & Loss Account	30,000
Advertisement Suspense Account	20,000
	50,000

Mohan surrenders $\frac{1}{3}$rd of $\frac{3}{5}$ in favour of Gopal, i.e., $\frac{1}{3} \times \frac{3}{5} = \frac{1}{5}$

Naresh surrenders $\frac{1}{4}$th of $\frac{2}{5}$ in favour of Gopal, i.e., $\frac{1}{4} \times \frac{2}{5} = \frac{1}{10}$

Hence, Sacrificing Ratio $= \frac{1}{5} : \frac{1}{10} = \frac{2:1}{10}$ or 2 : 1

Gopal's share $= \frac{1}{5} + \frac{1}{10} = \frac{2+1}{10} = \frac{3}{10}$

Adjustment Entry :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Mohan's Capital A/c ($\frac{2}{3}$ of 15,000)	Dr.		10,000	
	Naresh's Capital A/c ($\frac{1}{3}$ of 15,000)	Dr.		5,000	
	To Gopal's Current A/c ($\frac{3}{10}$ of 50,000)				15,000
	(Adjustment for accumulated losses on the admission of Gopal)				

ILLUSTRATION 87.

A, *B* and *C* are partners sharing profits and losses in the ratio of 5 : 4 : 1. They admitted *D* as a new partner and new profit sharing ratio is agreed at 3 : 4 : 2 : 3. They also decided to record the effect of the following without affecting their book values:

	₹
Contingency Reserve	1,00,000
Profit & Loss A/c	50,000
Advertisement Suspense A/c	30,000

You are required to give the necessary single journal entry.

SOLUTION :

Calculation of Net Effect of Accumulated Profits/Losses :

	₹
Contingency Reserve	1,00,000
(+) Profit & Loss A/c	50,000
	1,50,000
(–) Advertisement Suspense A/c	30,000
Net Effect	1,20,000

Calculation of Sacrifice or Gain :

Old Ratio – New Ratio

$A: \frac{5}{10} - \frac{3}{12} = \frac{30-15}{60} = \frac{15}{60}$ Sacrifice

$B: \frac{4}{10} - \frac{4}{12} = \frac{24-20}{60} = \frac{4}{60}$ Sacrifice

$C: \frac{1}{10} - \frac{2}{12} = \frac{6-10}{60} = \frac{4}{60}$ Gain

$D: \frac{3}{12}$ or $\frac{15}{60}$ Gain

Adjusting Entry :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	C's Capital A/c ($\frac{4}{60}$ of 1,20,000)	Dr.		8,000	
	D's Current A/c ($\frac{15}{60}$ of 1,20,000)	Dr.		30,000	
	To A's Capital A/c ($\frac{15}{60}$ of 1,20,000)				30,000
	To B's Capital A/c ($\frac{4}{60}$ of 1,20,000)				8,000
	(Adjustment for accumulated profits and losses on the admission of new partner D)				

ILLUSTRATION 88.

A and *B* are partners sharing profits and losses in the ratio of 3 : 2. *C* is admitted as a new partner for $\frac{1}{4}$th share which he acquires $\frac{1}{6}$th from *A* and $\frac{1}{12}$th from *B*. An extract of their Balance Sheet on this date is given below :

Liabilities	₹	Assets	₹
Workmen Compensation Reserve	60,000		

Partners agreed that the book value of any item appearing in the Balance Sheet is not to be altered and any adjustment on the admission of *C* is to be made by passing a single journal entry. Show the accounting treatment under the following alternative cases :

Case 1. If there is no other information.
Case 2. If a Claim for Workmen Compensation is estimated at ₹15,000
Case 3. If a Claim for Workmen Compensation is estimated at ₹60,000
Case 4. If a Claim for Workmen Compensation is estimated at ₹90,000

SOLUTION :

A sacrifices $\frac{1}{6}$ and *B* sacrifices $\frac{1}{12}$ from their Shares. Hence, Sacrificing Ratio $= \frac{1}{6} : \frac{1}{12}$ or 2 : 1.

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
Case 1	C's Current A/c ($60,000 \times \frac{1}{4}$)	Dr.		15,000	
	To A's Capital A/c ($15,000 \times \frac{2}{3}$)				10,000
	To B's Capital A/c ($15,000 \times \frac{1}{3}$)				5,000
	(Adjustment for Workmen Compensation reserve in sacrificing ratio of 2 : 1)				

Case 2	C's Current A/c $(45,000 \times \frac{1}{4})$ Dr.		11,250	
	To A's Capital A/c $(11,250 \times \frac{2}{3})$			7,500
	To B's Capital A/c $(11,250 \times \frac{1}{3})$			3,750
	(Adjustment for Workmen Compensation reserve of ₹60,000 *less* claim ₹15,000 in sacrificing ratio of 2 : 1)			
Case 3	No Entry			
Case 4	A's Capital A/c $(7,500 \times \frac{2}{3})$ Dr.		5,000	
	B's Capital A/c $(7,500 \times \frac{1}{3})$ Dr.		2,500	
	To C's Current A/c $(30,000 \times \frac{1}{4})$			7,500
	(Adjustment for Workmen Compensation Claim of ₹90,000 less reserve ₹60,000 in sacrificing ratio of 2 : 1)			

ILLUSTRATION 89.

X and *Y* sharing profits in the ratio of 3 : 2 admit *Z* as a new partner and the new profit sharing ratio is agreed at 2 : 1 : 1. An extract of their Balance Sheet as at that date is :

BALANCE SHEET

as at ....

Liabilities	₹	*Assets*	₹
Investment Fluctuation Reserve	40,000	Investments (at Cost)	3,00,000

Partners agreed that book value of any item of Balance Sheet is not to be altered and any adjustment is to be made by passing an adjustment entry. Show the accounting treatment under the following alternative cases :

Case 1. If there is no other information.
Case 2. If the market value of investments is ₹3,00,000
Case 3. If the market value of investments is ₹2,90,000
Case 4. If the market value of investments is ₹2,00,000
Case 5. If the market value of investments is ₹3,40,000

SOLUTION :

Calculation of Sacrificing Ratio :

$$X : \frac{3}{5} - \frac{2}{4} = \frac{12-10}{20} = \frac{2}{20}$$

$$Y : \frac{2}{5} - \frac{1}{4} = \frac{8-5}{20} = \frac{3}{20}$$

Thus, Sacrificing Ratio is 2 : 3.

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
Case 1	Z's Current A/c $(40,000 \times \frac{1}{4})$	Dr.		10,000	
	To X's Capital A/c $(10,000 \times \frac{2}{5})$				4,000
	To Y's Capital A/c $(10,000 \times \frac{3}{5})$				6,000
	(Adjustment for investment fluctuation reserve in sacrificing ratio of 2 : 3)				
Case 2	Same entry as given in Case 1				
Case 3	Z's Current A/c $(30,000 \times \frac{1}{4})$	Dr.		7,500	
	To X's Capital A/c $(7,500 \times \frac{2}{5})$				3,000
	To Y's Capital A/c $(7,500 \times \frac{3}{5})$				4,500
	(Adjustment for investment fluctuation reserve of ₹40,000 less ₹10,000 in sacrificing ratio of 2 : 3)				
Case 4	X's Capital A/c $(15,000 \times \frac{2}{5})$	Dr.		6,000	
	Y's Capital A/c $(15,000 \times \frac{3}{5})$	Dr.		9,000	
	To Z's Current A/c $(60,000 \times \frac{1}{4})$				15,000
	(Adjustment for fall in the value of investments ₹1,00,000 *less* investment fluctuation reserve ₹40,000)				
Case 5	Z's Current A/c $(80,000 \times \frac{1}{4})$	Dr.		20,000	
	To X's Capital A/c $(20,000 \times \frac{2}{5})$				8,000
	To Y's Capital A/c $(20,000 \times \frac{3}{5})$				12,000
	(Adjustment for investment fluctuation reserve of ₹40,000 plus ₹40,000 for increase in the value of investments)				

ILLUSTRATION 90.

A and *B* were partners in a firm sharing profits and losses in the ratio of 5 : 3. Their Balance Sheet as at 31st March, 2022 was as follows :

Liabilities		₹	Assets	₹
Capitals : *A*	2,00,000		Land and Building	3,50,000
B	1,00,000	3,00,000	Investments	
Workmen Compensation Reserve		25,000	(Market Value ₹90,000)	1,00,000
Contingency Reserve		75,000	Current Assets	1,40,000
Employee's Provident Fund		60,000	Advertisement Suspense A/c	

Investment Fluctuation Reserve	60,000	(Deferred Revenue	
Creditors	1,00,000	Expenditure)	30,000
	6,20,000		6,20,000

They admit *C* into partnership on 1st April, 2022 and the new profit sharing ratio is agreed at 7 : 5 : 4. It is estimated that claim on account of Workmen's Compensation is estimated at ₹40,000.

Partners do not want to alter the values given in the Balance Sheet but prefer to record the effect of change in profit sharing ratio by an adjustment entry. You are required to give the necessary journal entry.

SOLUTION :

(*i*) Adjustments to be made for :

		₹
	Contingency Reserve	75,000
	Investment Fluctuation Reserve	
	(₹60,000 *less* ₹10,000 for fall in the value of investments)	50,000
		1,25,000
Less :	Claim for Workmen Compensation	
	(₹40,000 *less* Workmen Compensation Reserve ₹25,000)	15,000
		1,10,000
Less :	Advertisement Suspense Account	30,000
		80,000

(*ii*) Sacrificing Ratio

$$A \ : \ \frac{5}{8} - \frac{7}{16} = \frac{10-7}{16} = \frac{3}{16}$$

$$B \ : \ \frac{3}{8} - \frac{5}{16} = \frac{6-5}{16} = \frac{1}{16}$$

Thus, Sacficing Ratio = 3 : 1

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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
April 1	C's Current A/c $(80{,}000 \times \frac{4}{16})$	Dr.		20,000	
	To *A*'s Capital A/c $(20{,}000 \times \frac{3}{4})$				15,000
	To *B*'s Capital A/c $(20{,}000 \times \frac{1}{4})$				5,000
	(Adjustment for accumulated profits and losses on C's admission)				

ILLUSTRATION 91.

A and *B* are partners sharing profits in the ratio of 3 : 2. Their balance sheet as at 31st March, 2022 is as under :

Liabilities		₹	*Assets*		₹
Sundry Creditors		90,000	Goodwill		50,000
General Reserve		1,10,000	Land and Building		5,40,000
Profit & Loss A/c		25,000	Investments (Market value ₹1,30,000)		1,50,000
Workmen Compensation Reserve		75,000	Stock		3,00,000
Investment Fluctuation Reserve		50,000	Debtors	1,80,000	
Capital Accounts :			*Less* : Provision for		
A	6,00,000		Doubtful Debts	25,000	1,55,000
B	3,00,000	9,00,000	Cash at Bank		25,000
			Advertisement Suspense A/c		30,000
		12,50,000			12,50,000

C is admitted into partnership. *A* sacrifices 1/3rd of his share and *B* sacrifices 1/10th from his share in favour of *C*.

Following terms are agreed upon :

(*i*) Goodwill is to be valued at 2 year's purchase of super profit of last 3 completed years, which were : 2020 ₹3,10,000, 2021 5,00,000 and 2022 4,80,000. The normal profit is ₹3,50,000 with the same amount of capital invested in similar business.

(*ii*) *C* brings ₹5,00,000 as capital and brings his share of goodwill premium in cash.

(*iii*) Accrued commission of ₹20,000 does not appear in the books and ₹25,000 are payable for rent.

(*iv*) Land and Building was found undervalued by 10%.

(*v*) Provision for Doubtful Debts is to be reduced to ₹10,000.

(*vi*) Claim on account of Workmen Compensation is ₹35,000.

(*vii*) After adjusting the Workmen Compensation Claim from Workmen Compensation Reserve and difference between book value and market value of investments from investment fluctuation reserve, remaining balance of such reserves and all accumulated profits/losses are to appear in the balance sheet of the new firm.

Prepare Revaluation Account, Partner's Capital Accounts and the Balance Sheet of the new firm.

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Outstanding Rent		25,000	By Accrued Commission	20,000
To Profit transferred to :			By Land & Building(3) (₹6,00,000 – ₹5,40,000)	60,000
A's Capital A/c	42,000			
B's Capital A/c	28,000	70,000	By Provision for Doubtful Debts	15,000
		95,000		95,000

PARTNER'S CAPITAL ACCOUNTS

Dr. Cr.

Particulars	A	B	C	Particulars	A	B	C
	₹	₹	₹		₹	₹	₹
To Goodwill (Written off)	30,000	20,000		By Balance b/d	6,00,000	3,00,000	
To Balance c/d	6,79,000	3,41,500	5,00,000	By Bank			5,00,000
				By Premium for Goodwill	32,000	16,000	
				By Revaluation	42,000	28,000	
				By C's Current A/c	35,000	17,500	
	7,09,000	3,61,500	5,00,000		7,09,000	3,61,500	5,00,000

BALANCE SHEET
as at 1st April, 2022

Liabilities		₹	Assets		₹
Sundry Creditors		90,000	Land and Building		6,00,000
Outstanding Rent		25,000	Investments		1,30,000
General Reserve		1,10,000	Stock		3,00,000
Profit & Loss Account		25,000	Debtors	1,80,000	
Workmen Compensation Claim		35,000	*Less :* Provision for Doubtful Debts	10,000	1,70,000
Workmen Compensation Reserve (₹75,000 – ₹35,000)		40,000	Accrued Commission		20,000
Investment Fluctuation Reserve (₹50,000 – ₹20,000)		30,000	Cash at Bank (25,000 + 5,00,000 + 48,000)		5,73,000
Capital Accounts :			Advertisement Suspense Account		30,000
A	6,79,000		C's Current Account		52,500
B	3,41,500				
C	5,00,000	15,20,500			
		18,75,500			18,75,500

Working Notes :

(1) (*i*) *A* has sacrificed $\frac{1}{3}$rd of $\frac{3}{5}$ in favour of *C*.

Hence, Sacrifice made by $A = \frac{1}{3} \times \frac{3}{5} = \frac{1}{5}$

(*ii*) *B* has sacrificed $\frac{1}{10}$th from his share

Hence, Sacrifice made by $B = \frac{1}{10}$

Sacrifice Ratio $= \frac{1}{5} : \frac{1}{10} = 2 : 1$

New Ratio $=$ A : $\frac{3}{5} - \frac{1}{5} = \frac{2}{5}$

B : $\frac{2}{5} - \frac{1}{10} = \frac{4-1}{10} = \frac{3}{10}$

$C \ : \ \frac{1}{5}+\frac{1}{10}=\frac{2+1}{10}=\frac{3}{10}$

Hence, New Ratio of A, B and $C = \frac{2}{5} : \frac{3}{10} : \frac{3}{10}$ or 4 : 3 : 3

(2) Calculation of Goodwill :

A. Average Profit $= \frac{3,10,000 + 5,00,000 + 4,80,000}{3} =$ ₹4,30,000

B. Normal Profit = ₹3,50,000

C. Super Profit = Average Profit – Normal Profit
= ₹4,30,000 – ₹3,50,000 = ₹80,000

D. Firm's Goodwill = Super Profit × No. of year's purchase
= ₹80,000 × 2 = ₹1,60,000

E. C's Share of Goodwill $= 1,60,000 \times \frac{3}{10} =$ ₹48,000

Journal Entries for Goodwill :

Bank A/c	Dr.	48,000	
To Premium for Goodwill A/c			48,000
Premium for Goodwill A/c	Dr.	48,000	
To A's Capital A/c $(48,000 \times \frac{2}{3})$			32,000
To B's Capital A/c $(48,000 \times \frac{1}{3})$			16,000

(3) Value of Land & Building $= 5,40,000 \times \frac{100}{90} =$ ₹6,00,000

(4) Adjustment for Accumulated Profits/Losses :

	₹
General Reserve	1,10,000
Profit & Loss Account	25,000
Workmen Compensation Reserve (₹75,000 – ₹35,000)	40,000
Investment Fluctuation Reserve (₹50,000 – ₹20,000)	30,000
	2,05,000
Less : Advertisement Suspense A/c	30,000
Net Amount	1,75,000

Adjustment Journal Entry :

C's Current A/c* $(1,75,000 \times \frac{3}{10})$	Dr.	52,500	
To A's Capital A/c $(52,500 \times \frac{2}{3})$			35,000
To B's Capital A/c $(52,500 \times \frac{1}{3})$			17,500

*C's Current Account should be debited instead of his Capital Account.

ILLUSTRATION 92.

X and *Y* are partners, sharing profits in the ratio of 7 : 5. They admit *Z* into the firm on 1st April, 2022, when their Balance Sheet was as follows :

Liabilities		₹	*Assets*		₹
Sundry Creditors		65,000	Land and Building		10,00,000
General Reserve		1,00,000	Debtors	2,00,000	
Profit & Loss Account		45,000	*Less :* Provision for Doubtful Debts	15,000	1,85,000
Workmen Compensation Reserve		60,000	Stock		44,000
Investment Fluctuation Reserve		30,000	Investments (Market value ₹2,15,000)		2,00,000
Capital Accounts :			Cash at Bank		46,000
X	8,00,000		Advertisement Suspense A/c		25,000
Y	4,00,000	12,00,000			
		15,00,000			15,00,000

Following terms are agreed :

(*i*) *X* will sacrifice $\frac{1}{24}$ from his share while *Y* sacrifices $\frac{3}{24}$ from his share in favour of *Z*.

(*ii*) *Z*'s share of Goodwill is valued at ₹1,20,000. *Z* brings ₹3,00,000 as Capital and brings 75% of his share of goodwill in cash.

(*iii*) Stock is found overvalued by 10%.

(*iv*) Provision for Doubtful Debts is to be made equal to 5% of the debtors.

(*v*) Value of Land and Building is to be brought upto 120% of its book value.

(*vi*) Claim on account of Workmen Compensation is ₹24,000.

Partners decided that general reserve, profit & loss account and advertisement suspense account are to appear in the books of the new firm at their original figures and necessary adjustment in this regard is to be made through Partner's Current Accounts.

Prepare Revaluation Account, Partner's Capital Accounts and the Balance sheet of the new firm. Also calculate new profit sharing ratios.

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Stock (₹44,000 – ₹40,000)(3)		4,000	By Provision for Doubtful Debts (₹15,000 – ₹10,000)	5,000
To Profit transferred to :			By Investments A/c	15,000
X's Capital A/c	1,26,000		By Land & Building	2,00,000
Y's Capital A/c	90,000	2,16,000		
		2,20,000		2,20,000

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*X*	*Y*	*Z*	*Particulars*	*X*	*Y*	*Z*
	₹	₹	₹		₹	₹	₹
To Balance c/d	9,94,500	6,07,500	3,00,000	By Balance b/d	8,00,000	4,00,000	
				By Bank A/c			3,00,000

				By Premium for Goodwill A/c	22,500	67,500	
				By Z's Current A/c (Goodwill)	7,500	22,500	
				By Revaluation A/c	1,26,000	90,000	
				By Workmen Compensation Reserve	21,000	15,000	
				By Investment Fluctuation Reserve	17,500	12,500	
	9,94,500	6,07,500	3,00,000		9,94,500	6,07,500	3,00,000

BALANCE SHEET
as at 1st April, 2022

Liabilities		₹	*Assets*		₹
Sundry Creditors		65,000	Land and Building		12,00,000
General Reserve		1,00,000	Debtors	2,00,000	
Profit & Loss Account		45,000	*Less :* Provision for		
Workmen Compensation Claim		24,000	Doubtful		
Capital Accounts :			Debts	10,000	1,90,000
X	9,94,500		Stock		40,000
Y	6,07,500		Investments		2,15,000
Z	3,00,000	19,02,000	Cash at Bank(7)		4,36,000
Current Accounts :			Advertisement Suspense A/c		25,000
X	5,000		*Z*'s Current A/c		
Y	15,000	20,000	(₹30,000 + ₹20,000)		50,000
		21,56,000			21,56,000

Working Notes :

(1) Share surrendered by $X = \frac{1}{24}$ and surrendered by $Y = \frac{3}{24}$

Hence, Sacrifice Ratio $= \frac{1}{24} : \frac{3}{24}$ or 1 : 3

New Ratio :

$$X : \frac{7}{12} - \frac{1}{24} = \frac{14-1}{24} = \frac{13}{24}$$

$$Y : \frac{5}{12} - \frac{3}{24} = \frac{10-3}{24} = \frac{7}{24}$$

$$Z : \frac{1}{24} + \frac{3}{24} = \frac{1+3}{24} = \frac{4}{24} \text{ or } \frac{1}{6}$$

Thus new ratio = 13 : 7 : 4

(2) **Journal Entries for Goodwill :**

Bank A/c (75% of ₹1,20,000)	Dr.	90,000	
To Premium for Goodwill			90,000
Premium for Goodwill A/c	Dr.	90,000	
To X's Capital A/c ($\frac{1}{4}$ of 90,000)			22,500
To Y's Capital A/c ($\frac{3}{4}$ of 90,000)			67,500
Z's Current A/c (₹1,20,000 – ₹90,000)	Dr.	30,000	
To X's Capital A/c ($\frac{1}{4}$ of 30,000)			7,500
To Y's Capital A/c ($\frac{3}{4}$ of 30,000)			22,500

(3) Value of Stock = ₹44,000 × $\frac{100}{110}$ = ₹40,000

(4) Excess Workmen Compensation Reserve ₹36,000 (*i.e.*, ₹60,000 – ₹24,000) will be transferred to Old Partner's Capital Accounts.

(5) Investment Fluctuation Reserve will be transferred to Old Partner's Capital Accounts.

(6) Adjustment for General Reserve, Profit & Loss Account and Advertisement Suspense Account :

	₹
General Reserve	1,00,000
Profit & Loss Account	45,000
	1,45,000
Less : Advertisement Suspense Account	25,000
Net Amount	1,20,000

Journal Entry for Adjustment :

Z's Current Account ($\frac{1}{6}$ of 1,20,000)	Dr.	20,000	
To X's Current A/c ($\frac{1}{4}$ of 20,000)			5,000
To Y's Current A/c ($\frac{3}{4}$ of 20,000)			15,000

Note : As per instructions given in the question, adjustment is to be made through Partner's Current Accounts.

(7)

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	46,000	By Balance c/d	4,36,000
To Z's Capital A/c	3,00,000		
To Premium for Goodwill A/c	90,000		
	4,36,000		4,36,000

ILLUSTRATION 93.

You are required to pass the necessary journal entries to carry out the following arrangements :

Antony and John are partners sharing profits in the ratio of 4 : 1. On 1st April, 2016, Ronny was admitted into their partnership for $\frac{1}{5}$th share in the profit which he acquired from Antony and John in the ratio of 3 : 1. Ronny brings in ₹30,000 as his capital and ₹20,000 as his share of goodwill. At the time of Ronny's admission, the firm had an Investment Fluctuation Reserve of ₹5,000 which the partners decided to show even in the reconstituted firm. Profit of the firm for the year ending 31st March, 2017 was ₹1,00,000. The firm followed the fixed capital method.

(I.S.C. Specimen Question Paper, 2018)

SOLUTION :

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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2016 April 1	Bank A/c	Dr.		50,000	
	To Ronny's Capital A/c				30,000
	To Premium for Goodwill A/c				20,000
	(Amount of capital and goodwill premium brought in cash)				
April 1	Premium for Goodwill A/c	Dr.		20,000	
	To Antony's Current A/c				15,000
	To John's Current A/c				5,000
	(Goodwill/premium credited to old partners in their sacrificing ratio of 3 : 1)				
April 1	Ronny's Current A/c (1/5th of ₹5,000)	Dr.		1,000	
	To Antony's Current A/c (3/4 of ₹1,000)				750
	To John's Current A/c (1/4 of ₹1,000)				250
	(Adjustment for Investment Fluctuation Reserve)				
2017 March 31	Profit & Loss Appropriation A/c	Dr.		1,00,000	
	To Antony's Current A/c				65,000
	To John's Current A/c				15,000
	To Ronny's Current A/c				20,000
	(Transfer of net profit in new profit sharing ratio of 13 : 3 : 4)				

Note : Calculation of New Profit Sharing Ratio :

Ronny acquires $= \frac{3}{4}$ of $\frac{1}{5}$ $= \frac{3}{20}$ from Antony

Ronny acquires $= \frac{1}{4}$ of $\frac{1}{5}$ $= \frac{1}{20}$ from John

Hence, the new ratio of Antony $= \frac{4}{5} - \frac{3}{20} = \frac{16-3}{20} = \frac{13}{20}$

new ratio of John $= \frac{1}{5} - \frac{1}{20} = \frac{4-1}{20} = \frac{3}{20}$

new ratio of Ronny $= \frac{1}{5}$

Hence, the new profit sharing ratio $= \frac{13}{20} : \frac{3}{20} : \frac{1}{5}$ or $\frac{13 : 3 : 4}{20} = 13 : 3 : 4$

ILLUSTRATION 94.

Annie and Bonnie are partners in a firm, sharing profits and losses equally. Their Balance Sheet as at 31st March, 2017 was as follows :

BALANCE SHEET OF ANNIE AND BONNIE
as at 31st March, 2017

Liabilities		*Amount*	*Assets*			*Amount*
		₹				₹
Sundry Creditors		21,000	Cash at Bank			20,000
General Reserve		15,000	Sundry Debtors		22,000	
Capital A/cs :			*Less :*	Provision for Doubtful Debts	(1,000)	21,000
Annie	45,000		Stock			10,000
Bonnie	40,000	85,000	Plant & Machinery			60,000
			Goodwill			10,000
		1,21,000				1,21,000

Carl was to be taken as a partner for $\frac{1}{4}$th share in the profits of the firm, with effect from 1st April, 2017 on the following terms :

(*a*) Bad Debts amounting to ₹1,500 to be written off.
(*b*) Stock to be taken over by Annie at ₹12,000.
(*c*) Plant and Machinery to be valued at ₹50,000.
(*d*) Goodwill of the firm to be valued at ₹20,000.
(*e*) Carl to bring in ₹50,000 as his capital. He was unable to bring in cash his share of goodwill.
(*f*) General Reserve not to be distributed. For this, it was decided that Carl would compensate the old partners through his current account.

You are required to :

(*i*) Pass journal entries on the date of Carl's admission.
(*ii*) Prepare the Capital Accounts and the Balance Sheet of the reconstituted firm.

(I.S.C. 2018)

SOLUTION : JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2017	Provision for Doubtful Debts A/c	Dr.		1,000	
April 1	Revaluation A/c	Dr.		500	
	To Sundry Debtors A/c				1,500
	(Bad Debts written off)				
	Stock A/c	Dr.		2,000	
	To Revaluation A/c				2,000
	(Increase in the value of Stock)				

Annie's Capital A/c	Dr.	12,000	
To Stock A/c			12,000
(Stock taken over by Annie)			
Revaluation A/c	Dr.	10,000	
To Plant and Machinery A/c			10,000
(Decrease in the value of Plant and Machinery)			
Annie's Capital A/c	Dr.	4,250	
Bonnie's Capital A/c	Dr.	4,250	
To Revaluation A/c			8,500
(Loss on revaluation transferred in old ratio)			
Annie's Capital A/c	Dr.	5,000	
Bonnie's Capital A/c	Dr.	5,000	
To Goodwill A/c			10,000
(Existing Goodwill written off in old ratio)			
Bank A/c	Dr.	50,000	
To Carl's Capital A/c			50,000
(Amount brought in by Carl for Capital)			
Carl's Current A/c	Dr.	5,000	
To Annie's Capital A/c			2,500
To Bonnie's Capital A/c			2,500
(Adjustment for Goodwill in sacrificing ratio)			
Carl's Current A/c	Dr.	3,750	
To Annie's Capital A/c			1,875
To Bonnie's Capital A/c			1,875
(Adjustment for general reserve in Sacrificing Ratio)			

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*Annie*	*Bonnie*	*Carl*	*Particulars*	*Annie*	*Bonnie*	*Carl*
	₹	₹	₹		₹	₹	₹
To Revaluation A/c	4,250	4,250		By Balance b/d	45,000	40,000	
To Stock A/c	12,000			By Bank			50,000
To Goodwill	5,000	5,000		By Carl's Current A/c	2,500	2,500	
To Balance c/d	28,125	35,125	50,000	By Carl's Current A/c	1,875	1,875	
	49,375	44,375	50,000		49,375	44,375	50,000

BALANCE SHEET OF ANNIE, BONNIE AND CARL
as at 1st April, 2017

Liabilities		Amount	*Assets*	Amount
		₹		₹
Sundry Creditors		21,000	Cash at Bank	70,000
General Reserve		15,000	Sundry Debtors	20,500
Capital A/c			Plant & Machinery	50,000
Annie	28,125		Carl's Current A/c	8,750
Bonnie	35,125			
Carl	50,000	1,13,250		
		1,49,250		1,49,250

SHORT ANSWER QUESTIONS

1. State two main rights acquired by a newly admitted partner. *(C.B.S.E. 2019)*

Ans. (*i*) Right to share the profits of the partnership firm.

(*ii*) Right to share the assets of the partnership firm.

2. Why should a new partner contribute towards goodwill on his admission?

Ans. Since a new partner gets his share of profits from old partners, he must compensate the old partners for the share sacrificed by them. The amount of compensation given by the new partner is known as goodwill.

3. State the ratio in which the old partners share the amount of cash brought in by the new partner as premium for goodwill.

Ans. The old partners share the amount of premium for goodwill in the sacrificing ratio because it is the amount of compensation to be paid by the new partner to old partners for acquiring the share of profits which they have surrendered in favour of new partner. It may, however, be mentioned that the old ratio itself will be the sacrificing ratio, in case the profit sharing ratio between the old partners remain unchanged.

4. Explain the accounting treatment of goodwill when no goodwill account appears in the books of the firm and the new partner brings his share of goodwill in cash.

Ans. First of all, amount of goodwill (usually known as premium for goodwill) is debited to 'Bank Account' and credited to 'Premium Account'. Thereafter, 'Premium Account' is debited and 'Old Partners Capital Accounts' are credited in sacrificing ratio. In case the whole or any portion of the premium is withdrawn by the old partners, their 'Capital Accounts' are debited and the 'Bank Account' is credited with the amount so withdrawn. When the new partner pays the amount of premium in cash to the old partners' privately outside the business, no entries are required to be passed.

5. Explain the accounting treatment of goodwill when goodwill account appears in the books of the firm and the new partner brings his share of goodwill in cash.

Ans. When a goodwill account already appears in the books of the firm, it must be written off by debiting the old Partner's Capital Accounts in their old profit sharing ratio and Crediting the Goodwill Account. Thereafter, first Bank Account will be debited and Premium Account will be credited and then Premium Account will be debited and Old Partner's Capital Accounts will be credited in sacrificing ratio. In case the whole or any portion of the premium is withdrawn by the old partners, their Capital Accounts are debited and the Bank Account is credited.

6. Explain the accounting treatment of goodwill when new partner cannot bring his share of goodwill in cash.

Ans. In such a case 'New Partners' Current Account' is debited with his share of goodwill and 'Old Partners' Capital Accounts' are credited in the sacrificing ratio.

7. What are accumulated profits?

Ans. The profits which have accumulated over the years and have not been credited to partner's capital accounts are called accumulated or undistributed profits such as General Reserve, Cr. balance of Profit & Loss Account etc.

8. What are accumulated losses?

Ans. The losses which have not been debited to partner's capital accounts are called accumulated or undistributed losses such as Debit balance of Profit & Loss Account appearing on the assets side of the Balance Sheet.

9. In case of admission of a new partner, give accounting treatment of accumulated profits and losses through one journal entry, when partners decide not to distribute such profit/loss.

Ans. *In case of Profits :*

Gaining Partner's Capital/Current A/cs (including new partner) Dr.
 To Sacrificing Partner's Capital/Current A/cs

In case of Losses :

Sacrificing Partner's Capital/Current A/cs (including new partner) Dr.
 To Gaining Partner's Capital/Current A/cs

10. State any two circumstances in which sacficing ratio may be applied.

Ans. (*i*) When there is a change in profit-sharing ratio.

(*ii*) When a new partner is admitted.

11. Why are accumulated profits and losses distributed amongst the old partners before a new partner is admitted?

Ans. If, at the time of admission, there are any accumulated profits and losses appearing in the balance sheet, they must be transferred to Old Partners' Capital Accounts in their old profit sharing ratio. The new partner should not share such profits or losses because these arose before his admission.

(I.S.C. 2009)

12. What is a Revaluation Account?

Ans. It is prepared to find out the profit or loss on revaluation of assets and liabilities at the time of reconstitution of the firm (i.e. change in profit sharing ratio, admission, retirement or death of a partner). Profit or loss shown by

revaluation account is divided between the old partners in old profit sharing ratio.

13. What is the nature of Revaluation Account?

Ans. It is a Nominal Account.

14. On the admission of a partner why are assets and liabilities revalued? *(I.S.C. 2001)*

Ans. At the time of admission of a new partner, the actual values of various assets and liabilities may be different from the values stated in the balance sheet. It is natural that the new partner should not benefit from any appreciation in the value of assets (or reduction in liabilities) nor should he suffer because of any fall in the value of assets (or increase in liabilities) which has occurred before his admission. Hence, assets and liabilities are revalued and the entire profit or loss arising from revaluation is divided between the old partners in their old profit sharing ratio.

15. State with reason whether at the time of admission of a partner, partnership is dissolved or partnership firm is dissolved.

Ans. Partnership is dissolved and not the firm because it is reconstitution of the firm under which the existing agreement comes to an end and a new one comes into existence.

16. Distinguish between Profit and Loss Appropriation Account and Profit and Loss Adjustment Account.

Ans. A Profit and Loss Appropriation Account, which is an extension of the Profit and Loss Account is prepared every year to show the distribution of profits (or losses) after dealing with the items, interest on capital, partner's salaries and interest on drawings. On the other hand, a Profit and Loss Adjustment Account is prepared only when a change in partnership constitution takes place, *e.g.*, admission, retirement etc. It is prepared to calculate the profit or loss on revaluation of assets and liabilities and to distribute such profit or loss amongst the partners.

17. If new partner brings in proportionate capital, how can it be calculated? Give a suitable example.

18. Under what circumstances premium for goodwill paid by the incoming partner would never be recorded in the books of account? *(I.S.C. 2003)*

Ans. When the incoming partner pays the amount of premium for goodwill in cash to the old partners privately outside the business, no entries are passed for it.

19. What is hidden goodwill and how is it calculated? *(I.S.C. 2004)*

Ans. When the value of goodwill of the firm is not given but has to be inferred on the basis of net worth of the firm, it is called hidden goodwill. Hidden goodwill is the excess of required capital of the firm over its actual combined capital of all partners.

For example, P and Q are partners with capitals of ₹1,00,000 each. R is admitted with $\frac{1}{4}$th share and he brings ₹1,20,000 as his capital. The Profit and Loss Account shows a credit balance of ₹50,000 on the date of admission of

R. On the basis of *R*'s capital, total capital of the firm should be ₹4,80,000 (₹1,20,000 × $\frac{4}{1}$). But the actual total capital of the firm is ₹3,70,000 (₹1,00,000 of *A* + ₹1,00,000 of *B* + ₹50,000 for Profit & Loss Account + ₹1,20,000 of *C*). As such, the Hidden Goodwill will be ₹1,10,000 (*i.e.*, ₹4,80,000 – ₹3,70,000).

20. How is goodwill paid privately by an incoming partner treated in the books of accounts? *(I.S.C. 2006)*

Ans. In such a case, no entry is passed in the books of the firm as it is a matter outside the firm.

21. State the two effects of the provisions of Accounting Standard-26 as issued by the Institute of Chartered Accountants of India. *(I.S.C. 2008)*

Ans. Recommendation of Accounting Standard-26

(1) Para 16 of Accounting Standard (AS) 26 specifies this goodwill can be recorded in the books only when some consideration in money or money's worth has been paid for it. It means that only purchased goodwill can be recorded in the books. At the time of admission, retirement or death of a partner or in case of change in profit sharing ratio among existing partners, **goodwill account cannot be raised** in the books of the firm because no consideration in money or money's worth has been paid for it.

(2) When the goodwill of the firm is evaluated and the new partner does not bring his share of goodwill in cash, goodwill should be adjusted through partner's capital accounts.

22. *P* and *Q* are partners sharing profits in the ratio of 5 : 3. *R* is admitted and the new ratio is 4 : 3 : 2. What will be the sacrificing ratio?

Ans. 13 : 3

23. Pawan and Jayshree are partners. Bindu is admitted for 1/4th share. What is the ratio in which Pawan and Jayshree will sacrifice their share in favour of Bindu?

Ans. Equally.

24. Karan, Nakul and Asha were partners in a firm sharing profits and losses in the ratio 3 : 2 : 1. At the time of admission of a partner, the goodwill of the firm was valued at ₹2,00,000. The accountant of the firm passed the entry in the books of accounts and thereafter showed goodwill ₹2,00,000 as an asset in the Balance Sheet. Is he correct in doing so? Why?

Ans. Accountant is not correct. As per AS-26, only purchased goodwill can be shown in the books. In this case, goodwill cannot be recorded because it is non-purchased goodwill and no consideration in money or money's worth has been paid for it.

25. List any two items that need adjustments in books of accounts of a firm at the time of admission of a partner.

Ans. (*i*) Adjustment for Goodwill.

(ii) Adjustment of Accumulated Profits, Reserves and Losses.

26. Atul and Neera were partners in a firm sharing profits in the ratio of 3 : 2. They admitted Mitali as a new partner. Goodwill of the firm was valued at ₹2,00,000. Mitali brings her share of goodwill premium of ₹20,000 in cash, which is entirely credited to Atul's Capital Account. Calculate the new profit sharing ratio.

Ans. New Ratio 5 : 4 : 1.

27. *S*, *T* and *U* were partners in a firm. They admitted *V* as a new partner. *S* and *T* sacrificed $\frac{1}{3}$rd and $\frac{1}{4}$th of their share respectively in favour of *V*. Calculate the new profit sharing ratio of *S*, *T*, *U* and *V*.

Ans. New Ratio 8 : 9 : 12 : 7.

28. *A* and *B* were partners in a firm sharing profits in the ratio of 3 : 2. *C* and *D* were admitted as new partners. *A* sacrificed $\frac{1}{4}$th of his share in favour of *C* and *B* sacrificed 50% of his share in favour of *D*. Calculate the new profit sharing ratio of *A*, *B*, *C* and *D*.

Ans. New Ratio 9 : 4 : 3 : 4.

29. *A* and *B* are partners in a firm. They admit *C* as a partner with 1/5th share in the profits of the firm. *C* brings ₹4,00,000 as his share of capital. Calculate the value of *C*'s share of Goodwill on the basis of his capital, given that the combined capital of *A* and *B* after all adjustments is ₹10,00,000.

(C.B.S.E. Sample Paper, 2020)

Ans.

		(₹)
Total Capital as per *C*'s Share	(4,00,000 × 5/1)	20,00,000
Less : Actual Capital of *A*, *B*, *C*	(10,00,000 + 4,00,000)	14,00,000
Value of Firm's Goodwill		6,00,000

C's share of Goodwill = 6,00,000 × 1/5 = ₹1,20,000

30. *A* and *B* are partners in a firm sharing profits and losses in the ratio of 3 : 2. On 1st April, 2019 they decided to admit *C* and their new ratio is decided to be equal. Pass the necessary journal entry to distribute Investment Fluctuation Reserve of ₹60,000 at the time of *C*'s admission, when Investment appear in the books at ₹2,10,000 and its market value is ₹1,90,000.

(C.B.S.E. Sample Paper, 2020)

Ans. JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019					
April 1	Investment Fluctuation Reserve A/c	Dr.		60,000	
	To Investment A/c				20,000
	To *A*'s Capital A/c				24,000
	To *B*'s Capital A/c				16,000
	(The transfer of excess investment fluctuation reserve to partner's capital accounts in old profit sharing ratio)				

31. A and B are in partnership sharing profits and losses in the ratio of 3 : 2. They admit C into partnership with 1/5th share which he acquires equally from A and B. Accountant has calculated new profit sharing ratio as 5 : 3 : 2. Is accountant correct? *(C.B.S.E. Sample Paper, 2020)*

Ans. C's Share acquired from A and B each $= \frac{1}{5} \times \frac{1}{2} = \frac{1}{10}$

A's Share $= \frac{3}{5} - \frac{1}{10} = \frac{5}{10}$

B's Share $= \frac{2}{5} - \frac{1}{10} = \frac{3}{10}$

New Profit Sharing Ratio of $A : B : C$ is 5 : 3 : 2

Yes, new profit sharing ratio is 5 : 3 : 2

32. A, B and C are partners sharing in the ratio of 3 : 2 : 1. They admit D for 1/4th share. It is agreed that B would retain his original share. New ratio will be .... *(C.B.S.E. Comptt. 2019)*

Ans. New Ratio : 15 : 16 : 5 : 12

Working :

B's share $= \frac{2}{6}$; D's share $= \frac{1}{4}$; Remaining Share $= 1 - \frac{2}{6} - \frac{1}{4} = \frac{5}{12}$

This will be divided between A and C in 3 : 1

A's new share $= \frac{5}{12} \times \frac{3}{4} = \frac{15}{48}$

C's new share $= \frac{5}{12} \times \frac{1}{4} = \frac{5}{48}$

New Share of A, B, C and $D = \frac{15}{48} : \frac{2}{6} : \frac{5}{48} : \frac{1}{4}$ or 15 : 16 : 5 : 12

OBJECTIVE TYPE QUESTIONS

(A) Fill in the blanks :—

(*i*) X and Y shared profits in the ratio of 3 : 1. They admit Z to one-third share in the future profits. The new profit sharing ratio will be ....

(*ii*) A, B and C are partners sharing profits in the ratio of 5 : 3 : 2. D is admitted for $\frac{1}{5}$ th share. The new profit sharing ratio will be ....

(*iii*) A and B who shared profits in the ratio of 3 : 1 admit C as a partner for $\frac{1}{5}$ th share in profits, which he acquires equally from the old partners. The new profit sharing ratio will be ....

(*iv*) A and B share profits in the ratio of 2 :1. C is admitted with $\frac{1}{3}$ rd share in profits. C acquires $\frac{2}{3}$ of his share from A and $\frac{1}{3}$ of his share from B. The new ratio will be ....

(*v*) X and Y are partners sharing profits in the ratio of 3 : 1. They admit Z as a partner. X surrenders $\frac{1}{3}$ rd of his share and Y $\frac{1}{4}$ th of his share in favour of Z. The new ratio will be ....

(*vi*) P and Q are partners sharing profits in the ratio of 5 : 3. R is admitted and the new ratio is 4 : 3 : 2. The sacrificing ratio is ....

(*vii*) A, B and C share profits in the ratio of 5 : 4 : 3. D is admitted for 1/4 th share. The sacrificing ratio will be ....

(*viii*) Decrease in provision for doubtful debts will be .... to Revaluation A/c.

(*ix*) Old ratio is itself .... ratio, unless otherwise stated.

(*x*) On the admission of a new partner, goodwill brought in cash is always distributed among old partners in the .... ratio.

(*xi*) On the admission of a new partner, decrease in the value of an asset is debited to .... Account

(*xii*) On the admission of a new partner decrease in the value of a liability is .... to Revaluation Account.

[**Ans.**	(*i*) 3 : 1 : 2	(*ii*) 10 : 6 : 4 : 5	(*iii*) 13 : 3 : 4
	(*iv*) 4 : 2 : 3	(*v*) 8 : 3 : 5	(*vi*) 13 : 3
	(*vii*) 5 : 4 : 3	(*viii*) Credited	(*ix*) Sacrificing
	(*x*) Sacrificing	(*xi*) Revaluation	(*xii*) Credited]

(B) State whether each of the following Statements is True or False?

(*i*) Goodwill is always distributed among old partners in the sacrificing ratio.

(*ii*) Profit or loss on revaluation is transferred to old partner's capital accounts in their sacrificing ratio.

(*iii*) A new partner may be admitted to a partnership only with the consent of all the old partners.

(*iv*) New profit sharing ratio minus old profit sharing ratio is known as sacrificing ratio.

(*v*) Accumulated profit or loss is transferred to all partner's capital accounts including new partner.

(*vi*) On the admission of a new partner, general reserve appearing in the Balance Sheet is transferred to Revaluation Account.

(*vii*) On the admission of a new partner, if the profit sharing ratio of a partner remains unchanged he will not be entitled to any amount of goodwill brought in cash by the new partner.

(*viii*) Adjustment of Capital in the profit sharing ratio or on the basis of new partner's capital are the same thing.

(*ix*) Revaluation Account is debited for increase in the value of a liability.

[**Ans.** True : (*i*); (*iii*); (*vii*); (*viii*); (*ix*).]

PRACTICAL QUESTIONS

(Questions Nos. 1 to 92 are strictly in the serial order of Illustrations)

New Profit Sharing Ratio

Q. 1 (A). *A* and *B* are partners sharing profits in the ratio of 5 : 3. *C* is admitted to the partnership for 1/4th share of future profits. Calculate the new profit sharing ratio.

[**Ans.** New Ratio 15 : 9 : 8.]

Q. 1 (B). *A* and *B* were partners sharing profits in the ratio of 21 : 9. *C* was admitted on 9/21 share in the profits. Calculate new profit sharing ratio of the partners.

[**Ans.** New Ratio 14 : 6 : 15.]

Q. 2 (A). *P* and *Q* are partners sharing profits and losses in the ratio of 4 : 3. They admit *R* as partner for a 1/7th share in profits which he acquires equally from *P* and *Q*. Calculate new profit sharing ratio of the partners.

[**Ans.** 7 : 5 : 2.]

Q. 2 (B). *P*, *Q* and *R* were partners in a firm sharing profits in the ratio of 3 : 2 :1. They admitted *S* as a new partner for 1/8th share in the profits which he acquired 1/16th from *P* and 1/16th from *Q*. Calculate new profit sharing ratio of *P*, *Q*, *R* and *S*.

[**Ans.** New Ratio 21 : 13 : 8 : 6.]

Q. 3 (A). *X* and *Y* are partners sharing profits in the ratio of 2 : 1. *Z* is admitted with 5/11th share which he takes 3/11th from *X* and 2/11th from *Y*. Calculate the new profit sharing ratio of the partners.

[**Ans.** 13 : 5 : 15.]

Q. 3 (B). *A* and *B* are partners sharing profits in the ratio of 5 : 3. They admit *C* on 1/4th share which he acquires 1/6th from *A* and 1/12th from *B*. Calculate the new profit sharing ratio of the partners.

[**Ans.** 11 : 7 : 6.]

Q. 4. *A* and *B* are partners sharing profits in the ratio of 3 : 2. They admit *C* into partnership giving him 1/2 share in profits which he acquires from *A* and *B* in the ratio of 3 : 1. Calculate the new profit ratio.

[**Ans.** New Ratio 9 : 11 : 20.]

Q. 5. *X* and *Y* are partners sharing profits and losses in the ratio of 3 : 2. They admit *Z* as a new partner who gets 1/5th share. Calculate the new profit sharing ratio in each of the following cases :

(*i*) If *Z* acquires his share from *X* and *Y* in their profit sharing ratio; (*ii*) If he acquires 3/20th from *X* and 1/20th from *Y*; (*iii*) If he acquires 1/10th from *X* and 1/10th from *Y*; (*iv*) If he acquires 1/20th from *X* and 3/20th from *Y*; (*v*) If he acquires his share entirely from *X*; (*vi*) If he acquires his share entirely from *Y*.

[**Ans.** (*i*) 12 : 8 : 5; (*ii*) 9 : 7 : 4; (*iii*) 5 : 3 : 2; (*iv*) 11 : 5 : 4; (*v*) 2 : 2 : 1 and (*vi*) 3 : 1 : 1.]

Q. 6. *A*, *B* and *C* are partners in a firm sharing profits in 4 : 3 : 3 ratio. They decided to admit their manager *D* into partnership. *A* surrendered $\frac{1}{4}$ of his share in favour of *D*; *B* surrendered $\frac{1}{5}$ of his share in favour of *D* and *C* surrendered $\frac{1}{6}$ of his share in favour of *D*. Calculate new profit sharing ratio.

[**Ans.** 30 : 24 : 25 : 21]

Q. 7. *A* and *B* are partners sharing profits and losses in the ratio of 3 : 2. They admit *X* and *Y* as new partners. *A* surrendered 1/3rd of his share in favour of *X* and *B* surrendered 1/4th of his share in favour of *Y*. Calculate the new profit sharing ratio of *A, B, X* and *Y*.

[**Ans.** New Ratio of *A, B, X* and *Y* = 4 : 3 : 2 : 1.]

Q. 8. *A* and *B* share profits and losses in the ratio of 3 : 2. They admit *C* as a new partner for $\frac{1}{3}$rd share in the profits of the firm which he acquired from *A* and *B* in the ratio of 2 : 3. After some time, they admitted *D* as a new partner for $\frac{1}{5}$th share in the profits which he acquired equally from *A* and *C*.

Calculate :

(*i*) New profit sharing ratio of *A, B* and *C*;

(*ii*) New profit sharing ratio of *A, B, C* and *D*.

[**Ans.** (*i*) 7 : 3 : 5; (*ii*) 11 : 6 : 7 : 6]

Q. 9. *P* and *Q* share profits in 3 : 2. They admit *R* and *S* with $\frac{1}{4}$ and $\frac{1}{5}$ share respectively. Calculate the new ratios of partners.

[**Ans.** New Ratios 33 : 22 : 25 : 20]

Sacrificing Ratios and New Ratios

Q. 10. *A, B* and *C* share profit and losses in the ratio of 3 : 2 : 1. Upon admission of *D*, they agreed to share as follows :

(*i*) 4 : 4 : 2 : 2

(*ii*) 2 : 4 : 2 : 4

Calculate sacrificing ratios.

[**Ans.** (*i*) Only *A* sacrifices = $\frac{1}{6}$; (*ii*) Only *A* sacrifices = $\frac{2}{6}$.]

Q. 11. *A* and *B* are partners sharing profit in the ratio of 5 : 3. *C* is admitted to the partnership for 1/4th share of future profits. Calculate the new profit sharing ratio and the sacrificing ratio.

[**Ans.** New Ratio = 15 : 9 : 8, Sacrificing ratio = 5 : 3.]

Q. 12. *A* and *B* are partners sharing profits in the ratio of 7 : 3. *C* was admitted. *A* surrendered 1/7th of his share and *B* 1/3rd of his share in favour of *C*. Calculate the sacrificing ratio and the new profit-sharing ratios of the partners.

[**Ans.** Sacrificing Ratio 1 : 1; New Ratio 3 : 1 : 1.]

Q. 13 (A). *A* and *B* are partners in a firm sharing profits and losses in the ratio of 3 : 2. *C* is admitted into partnership. *A* sacrifices 1/3 of his share and *B* $\frac{1}{10}$ from his share in favour of *C*. Determine the sacrificing ratio and the new profit sharing ratio.

[**Ans.** Sacrifice Ratio 2 : 1; New Ratio 4 : 3 : 3.]

Q. 13 (B). *A* and *B* are partners in a firm sharing profits and losses in the ratio of 5 : 3. They admit *C* and *D* as new partners. *A* sacrifices $\frac{1}{2}$ of his share in favour of *C* and *B* sacrifices $\frac{1}{4}$ from his share in favour of *D*. Calculate their new profit sharing ratio.

[**Ans.** New Ratio 5 : 2 : 5 : 4]

Q. 14. *A, B, C* and *D* are in partnership sharing profits and losses in the ratio of 36 : 24 : 20 : 20 respectively. *E* joins the partnership for 20% share, *A, B, C* and *D* would in future share profits among themselves as 3/10 : 4/10 : 2/10 and 1/10. Calculate the new profit sharing ratio after *E*'s admission.

[**Ans.** New Ratio 6 : 8 : 4 : 2 : 5]

Q. 15. *A* and *B* are partners in a firm sharing profits in the ratio of 3 : 1. They admit *C* and decide that the profit-sharing ratio between *B* and *C* shall be same as existing between *A* and *B*. Calculate new profit-sharing ratio and the sacrificing ratio.

[**Ans.** New Ratio 9 : 3 : 1; Sacrificing Ratio = 3 : 1.]

Q. 16. *A, B* and *C* are partners sharing in the ratio of 4 : 3 : 2. They admit *D* for 1/9th share. It is agreed that *A* would retain his original share. Calculate the new ratios and sacrificing ratios.

[**Ans.** New Ratio 20 : 12 : 8 : 5; Sacrificing Ratio between *B* and *C* 3 : 2.]

Q. 17. *P, Q* and *R* are partners sharing profits and losses in the ratio of 5 : 3 : 2. *S* is admitted as a new partner for $\frac{1}{5}$th share. *P* sacrifices $\frac{1}{10}$th from his share in favour of *S* and remaining sacrifice was made by *Q* and *R* in the ratio of 2 : 1. Calculate sacrificing ratio and new profit sharing ratio.

[**Ans.** Sacrificing Ratio 3 : 2 : 1; New Ratio 12 : 7 : 5 : 6]

When new partner brings goodwill/premium in cash

Q. 18. *L, M* and *N* are partners sharing profits in the ratio of 3 : 2 : 1. They admit *O* into partnership. *O* brings in cash ₹4,50,000 as capital and ₹1,50,000 as goodwill for 1/5th share of profits. Pass journal entries and find out new profit sharing ratios when : (*a*) Goodwill is retained in the firm; (*b*) goodwill is withdrawn by old partners.

[**Ans.** New Profit sharing ratio = 6 : 4 : 2 : 3.]

Q. 19. *P* and *Q* are partners sharing profits and losses in the ratio of 2 : 1. They admit *R* into partnership for 4/9th share in profits which he acquires equally from *P* and *Q*. *R* brings in cash ₹2,50,000 as capital and ₹1,80,000 as goodwill.

Pass journal entries and find out new profit sharing ratios.

[**Ans.** New profit sharing ratio is 4 : 1 : 4.]

Q. 20 (A). *X* and *Y* are partners sharing profits in the ratio of 4 : 3. *Z* joins partnership for 2/7th share in the profits (of which he acquires 3/4th from *X* and 1/4th from *Y*). *Z* brings in ₹3,00,000 for his capital and ₹1,20,000 for goodwill. Half of the amount of goodwill is withdrawn by the old partners.

Pass necessary Journal entries and find out new profit sharing ratio.

[**Ans.** New profit sharing ratio is 5 : 5 : 4.]

Q. 20 (B). *K* and *Y* were partners in a firm sharing profits in 3 : 2 ratio. They admitted *Z* as a new partner for 1/3rd share in the profits of the firm. *Z* acquired his share from *K* and *Y* in 2 : 3 ratio. *Z* brought ₹80,000 for his capital and ₹30,000 for his 1/3rd share as premium. Calculate the new profit sharing ratio of *K*, *Y* and *Z* and pass necessary journal entries for the above transactions in the books of the firm.

[**Ans.** New profit sharing ratio = 7 : 3 : 5]

Q. 21. Anju and Manju are partners, sharing profits and losses in the proportion of 7 : 5. They agreed to admit Meenu, their manager, into partnership, who is to get one sixth share in the business. Meenu brings in ₹2,00,000 for her capital and ₹96,000 for 1/6th share of goodwill which she acquires 1/24th from Anju and 1/8th from Manju. The profit for the first year of the new partnership amount to ₹4,80,000.

Make the necessary Journal entries in connection with Meenu's admission and divide the profit between the partners.

[**Ans.** New profit sharing Ratio 13 : 7 : 4; Profit : Anju ₹2,60,000; Manju ₹1,40,000 and Meenu ₹80,000.]

Q. 22. *X* and *Y* share profits and losses in the ratio of 3 : 2. They admit *Z* as a partner who pays ₹72,000 as premium for goodwill for 1/4th share in the future profits of the firm.

Pass Journal entries appropriating the premium money and show the new profit sharing ratio in each of the following cases :

(*i*) if he acquires his share of profits in the original ratio of existing partners.

(*ii*) if he acquires his share of profits in equal proportions from the existing partners.

(*iii*) if he acquires his share in the ratio of 2 : 3 from the existing partners.

(*iv*) if he acquires his share of profits as $\frac{7}{32}$th from *X* and $\frac{1}{32}$th from *Y*.

[**Ans.** New Ratio : Case (*i*) 9 : 6 : 5 Case (*ii*) 19 : 11 : 10
Case (*iii*) 2 : 1 : 1 Case (*iv*) 61 : 59 : 40
Sacrificing Ratio for goodwill distribution :
Case (*i*) 3 : 2 Case (*ii*) 1 : 1
Case (*iii*) 2 : 3 Case (*iv*) 7 : 1]

Q. 23. Partners *A*, *B* and *C* share the profit of a business in the ratio of 3 : 2 : 1 respectively. For one-sixth share they admit *D* who brings in ₹2,00,000 including ₹60,000 for his share of goodwill. Show the journal entries if *A*, *B*, *C* and *D* decide to

share the profits respectively in the ratio of (*a*) 15 : 10 : 5 : 6; (*b*) 5 : 3 : 2 : 2 and (*c*) 2 : 2 : 1 : 1. Assume that the entire cash brought in by *D* remains in the business. Give Journal entries.

[**Ans.** Sacrificing Ratio : (*a*) 3 : 2 : 1, (*b*) *A* : *B* = 1 : 1; (*c*) Only *A* sacrifices.]

Q. 24 (A). *P* and *Q* are partners sharing profits in the ratio of 7 : 5. They admit *R* into partnership for 1/4 share who pays ₹30,000 in cash for goodwill. *P* and *Q* decide to share future profits equally among themselves. Pass entries.

[**Ans.** New Ratio 3 : 3 : 2; premium for goodwill ₹30,000 will be distributed in the sacrifice ratio of 5 : 1.]

Q. 24 (B). *X* and *Y* are partners sharing profits and losses in the ratio of 2 : 1. They agree to admit *Z* into partnership who gets 1/3rd share in the profits. *Z* brings in ₹50,000 for his capital and the necessary amount for goodwill in cash. Goodwill of the firm is valued at ₹36,000. *X, Y* and *Z* agree to share future profits equally. The amount of goodwill is withdrawn from the business. Pass entries.

[**Ans.** Premium for goodwill brought in by *Z* ₹12,000 will be credited to *X*'s Capital A/c, as he alone has sacrificed.]

Q. 25. *A*, *B* and *C* are partners sharing profits and losses in the ratio of 3 : 2 : 1. They admit *D* for $\frac{1}{4}$th share in the profits and he brought in ₹1,50,000 as his share of goodwill which was credited to the Capital Accounts of *B* and *C* respectively with ₹1,25,000 and ₹25,000.

Calculate the new profit sharing ratio.

[**Ans.** New Ratio 4 : 1 : 1 : 2.]

Q. 26. *A* and *B* are partners sharing profits and losses as 2 : 1. On 1st April, 2020 they admit *C* as a partner for 1/4th share who pays ₹4,50,000 as goodwill privately. On 1st April, 2021, they take *D* as a partner for 3/5th share who brings ₹4,00,000 as goodwill, out of which half is withdrawn by the existing partners. On 1st April, 2022, *E* is admitted as a partner for 1/6th share who brings ₹5,00,000 as goodwill which is retained in the business.

Journalise the above transactions in the books of the firm.

[**Ans.** New profit sharing ratios : 2020 — 2 : 1 : 1; 2021 — 2 : 1 : 1 : 6; and 2022 — 2 : 1 : 1 : 6 : 2.]

Q. 27. *P* and *Q* are partners sharing profits & losses as 2 : 3. *R* and S are admitted and profit sharing ratio becomes 3 : 4 : 3 : 2. Goodwill is valued at ₹3,00,000. *R* brings required goodwill and ₹2,00,000 cash for Capital. *S* brings in ₹1,00,000 cash and Motor Vehicle for ₹80,000 as his capital in addition to the required amount of goodwill in cash.

Show the necessary journal entries.

[**Ans.** Sacrificing Ratio 9 : 16]

Q. 28. Asha and Aditi are partners in a firm sharing profits and losses in the ratio of 3 : 2. They admit Raghav as a partner for 1/4th share in the profits of the firm. Raghav brings ₹6,00,000 as his capital and his share of goodwill in cash. Goodwill of the firm is to be valued at two years' purchase of average profits of the last four years.

The profits of the firm during the last four years are given below :

Year	Profit (₹)
2013–14	3,50,000
2014–15	4,75,000
2015–16	6,70,000
2016–17	7,45,000

The following additional information is given :

(*i*) To cover management cost an annual charge of ₹56,250 should be made for the purpose of valuation of goodwill.

(*ii*) The closing stock for the year ended 31.3.2017 was overvalued by ₹15,000.

Pass necessary journal entries on Raghav's admission showing the working notes clearly. *(C.B.S.E. 2018)*

[**Ans.** Raghav's share of goodwill : ₹2,50,000.]

Q. 29 (A). *A* and *B* are partners, sharing profit and losses in the ratio of 3 : 2. Goodwill appears in their Balance Sheet at ₹24,000, when *C* is admitted into partnership for 1/5th share in profit. He pays ₹50,000 for capital and ₹8,000 as goodwill. The ratio of the partners *A*, *B* and *C* in the new firm would be 2 : 2 : 1.

Pass journal entries in the books of the new firm to record above adjustments.

[**Ans.** Premium for goodwill ₹8,000 is transferred to *A*'s capital.

Old goodwill ₹24,000 will be written off in *A* and *B* in the ratio of 3 : 2.]

Q. 29 (B). *A* and *B* carrying on business as partners used to share profits and losses thus; *A* 4/7ths and *B* 3/7ths, and goodwill appeared in the books of the firm at ₹2,80,000 when *C* was admitted as a partner having 1/7th share in profits and losses. *C* was asked to pay a premium of ₹75,000 for goodwill, and the profit-sharing ratio as between *A* and *B* remained unchanged.

Show entries in the journal of the firm.

[**Ans.** Goodwill of ₹2,80,000 written off by *A* and *B* in their old ratio *i.e.* 4 : 3.]

When New Partner does not bring Goodwill/premium in Cash

Q. 30. *A* and *B* are partners sharing profits in the ratio of 4 : 3. *C* is admitted into the partnership and the new ratio is determined at 3 : 2 : 1. *C* does not pay anything for his share of goodwill. On *C*'s admission firm's goodwill was valued at ₹84,000. Pass journal entry.

[**Ans.** *C*'s Current Account will be debited by ₹14,000 and Capital Accounts of *A* and *B* will be credited in their sacrificing ratio *i.e.*, 3 : 4.]

Q. 31. *A*, *B* and *C* were partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. They admit *D* into partnership with $\frac{1}{4}$th share which he acquires from *A* and *B* in the ratio of 2 : 1. On *D*'s admission the goodwill of the firm is valued at ₹6,00,000. However, *D* is unable to bring his share of goodwill in cash.

Pass necessary journal entry and also calculate the new profit sharing ratio.

[**Ans.** New Ratio 4 : 3 : 2 : 3. Entry for Goodwill :

D's Current A/c	Dr.	1,50,000	
To *A*'s Capital A/c			1,00,000
To *B*'s Capital A/c			50,000]

Q. 32. *A* and *B* are partners sharing profits in the ratio of 3 : 2. On 1st April, 2022 they admit *C* as a new partner for $\frac{1}{4}$th share. *C* acquires $\frac{1}{5}$th of his share from *A*.

Goodwill on *C*'s admission is to be valued on the basis of capitalisation of average profits of the last five years. Profits were :

Year ended
31st March, 2018 Profit ₹50,000
31st March, 2019 Profit ₹1,20,000 (including gain of ₹40,000 from sale of fixed assets)
31st March, 2020 Loss ₹60,000 (after charging Loss by Fire ₹50,000)
31st March, 2021 Loss ₹1,00,000 (after charging voluntary retirement compensation paid ₹1,50,000)
31st March, 2022 Profit ₹1,90,000

On 1st April, 2022, the firm had assets of ₹7,00,000 and external liabilities of ₹2,20,000.

The normal rate of return on capital is 12%.

C brings in ₹1,25,000 for his capital but is unable to bring his share of goodwill in cash.

(*i*) You are required to calculate *C*'s share of goodwill,

(*ii*) Pass necessary journal entries, and

(*iii*) Calculate new profit sharing ratios.

[**Ans.** *C*'s share of Goodwill ₹30,000; Sacrificing Ratio 1 : 4; New Profit Sharing Ratio 11 : 4 : 5]

Hint. *C* acquires $\frac{1}{5}$th of his share from *A* and remaining $\frac{4}{5}$th of his share from *B*.

Q. 33. *P*, *Q* and *R* share profits in the ratio of 5 : 3 : 2. *S* was admitted into partnership. *S* brings in ₹30,000 as his capital. *S* is entitled for 1/5th share in profits which he acquires equally from *P*, *Q* and *R*. Goodwill of the firm is to be valued at three years' purchase of last four years' average profits. The profits of the last four years' are ₹32,000, ₹38,000, ₹35,000 and ₹31,000 respectively. *S* cannot bring goodwill in cash. Goodwill already appears in the books at ₹50,000. Give Journal entries.

[**Ans.** Existing Goodwill of ₹50,000 will be written off among *P*, *Q* and *R* in 5 : 3 : 2. Current A/c of *S* will be debited by his share of goodwill ₹20,400 and Capital Accounts of *P*, *Q* and *R* will be credited in equal proportion.]

Q. 34. *X* and *Y* are partners sharing profits in the ratio of 3 : 2. Goodwill appears in their balance sheet at ₹60,000. *Z* is admitted as a partner for 1/4th share in the profits. The total goodwill of the firm is valued at ₹2,00,000.

Pass journal entries if :

1. *Z* cannot bring in cash his share of goodwill.

2. Z brings in cash his share of goodwill.

Hint. In both cases, goodwill appearing in the balance sheet at ₹60,000 will be written off between old partners in old ratio.

Q. 35. X, Y and Z were partners sharing profits and losses as to X one-half; Y one-third; and Z one-sixth. As from 1st April, 2020, they agreed to admit A into partnership for one-sixth share in profits and losses, which he acquires equally from X and Y, and is to bring in ₹50,000 for his capital and ₹20,000 as premium for goodwill. A paid in his capital money but in respect of premium for goodwill, he could bring in only ₹15,000.

You are required to :

(*i*) give the Journal entries to carry out the above arrangements, and

(*ii*) work out the new profit-sharing ratio of the partners.

[**Ans.** New Ratio 5 : 3 : 2 : 2]

Hint. Premium for Goodwill A/c will be debited by ₹15,000 and Current A/c of A will be debited by ₹5,000 and Capital A/cs of X and Y will be credited by ₹10,000 each.

Q. 36. A and B are partners sharing profits in the ratio of 5 : 3. They admit C into the firm for 3/10th profit which he takes 2/10th from A and 1/10th from B and brings ₹1,50,000 as premium in Cash out of his share of ₹3,90,000. Goodwill account does not appear in the books of A and B. Give journal entries and the new ratio of A, B and C.

[**Ans.** New ratio 17 : 11 : 12.]

Hint. Premium for Goodwill A/c will be debited by ₹1,50,000 and Current Account of C will be debited by ₹ 2,40,000 and Capital Accounts of A and B will be credited by ₹2,60,000 and ₹1,30,000 respectively.

Q. 37. A and B are partners sharing profits in the ratio of 3 : 1. C is admitted as a partner with 2/9th share; A and B will in future get 4/9th and 3/9th share of profits. C pays ₹20,000 for goodwill. Pass the necessary journal entries.

[**Ans.** A sacrifices 11/36 whereas B gains 3/36 and C gains 8/36. Hence Premium for Goodwill A/c will be debited by ₹20,000 and B's Capital A/c will be debited by ₹7,500 and A's Capital A/c will be credited by ₹27,500.]

Q. 38. X and Y are partners sharing profits in the ratio of 3 : 1. Z is admitted as a partner for which he pays ₹30,000 for goodwill in cash. X, Y and Z decided to share future profits in equal proportion. You are required to pass a single journal entry to give effect to the above.

[**Ans.** X sacrifices $\frac{5}{12}$ whereas Y gains $\frac{1}{12}$ and Z gains $\frac{1}{3}$. Entry will be :

Premium for Goodwill A/c	Dr.	30,000	
Y's Capital A/c	Dr.	7,500	
To X's Capital A/c			37,500]

Q. 39. Mohan, Naresh and Om were in partnership sharing profits and losses in the ratio of 10 : 4 : 1. On 1st April, 2021 their capitals were ₹3,00,000; ₹1,50,000 and ₹50,000 respectively. On this date they admit Piyush as a new partner and the new profit sharing ratio is agreed at 5 : 4 : 4 : 2. The following terms were also agreed upon:

(*i*) Piyush will bring in ₹40,000 as his capital.

(*ii*) He will also bring in his share of goodwill in cash. Goodwill is to be valued on the basis of capitalisation at 10% of the average profits of the last three years. Profits of the last three years were :

	₹
Year ended 31st March 2019	48,000
Year ended 31st March 2020	75,000
Year ended 31st March 2021	72,000

(*iii*) The new partner is entitled to an annual salary of ₹7,500 in addition to his share of profit. Om personally guaranteed that Piyush's share of profit shall not be less than ₹30,000.

Profits for the year ended 31st March 2022 amounted to ₹2,10,000 before charging Piyush's salary.

Prepare necessary entries at the time of admission of the new partner and show the distribution of profits for the year ended 31st March, 2022.

[**Ans.** Value of Goodwill ₹1,50,000; Om gains $\frac{3}{15}$th share. Hence Om will be debited and Mohan will be credited by ₹30,000 plus ₹20,000 brought in by Piyush. Share of Profit : Mohan ₹67,500; Naresh ₹54,000, Om ₹51,000 and Piyush ₹30,000.]

Revaluation of Assets and Liabilities

Q. 40. Pass journal entries to record the following transactions on the admission of a new partner :

(*i*) Land and Building is undervalued by ₹2,00,000.

(*ii*) Stock is overvalued by 20% (Book Value of Stock ₹60,000).

(*iii*) Provision to be made for compensation of ₹20,000 to an ex-employee.

(*iv*) Sundry Debtors appeared in the books at ₹1,50,000. They are estimated to produce not more than ₹1,30,000.

(*v*) Creditors include an amount of ₹10,000 received as commission.

(*vi*) A bill of exchange of ₹40,000 which was previously discounted with the banker, was dishonoured on 31st March, 2022 but no entry has been passed for it.

(*vii*) Value of Machinery is to be decreased to ₹1,20,000 (Book Value ₹2,00,000).

(*viii*) Value of Machinery is to be decreased by ₹1,20,000 (Book Value ₹2,00,000).

(*ix*) Expenses on revaluation amount to ₹8,000 have been paid by partner *X*.

[**Ans.**

(*i*) Dr. Land & Building A/c; Cr. Revaluation A/c by ₹2,00,000.

(*ii*) Dr. Revaluation A/c; Cr. Stock A/c by ₹10,000.

(*iii*) Dr. Revaluation A/c; Cr. Provision for Compensation by ₹20,000.

(*iv*) Dr. Revaluation A/c; Cr. Provision for Doubtful Debts A/c by ₹20,000.

(*v*) Dr. Creditors A/c; Cr. Revaluation A/c by ₹10,000.

(*vi*) Dr. Sundry Debtors A/c; Cr. Bank A/c by ₹40,000.

(*vii*) Dr. Revaluation A/c; Cr. Machinery A/c by ₹80,000.

(*viii*) Dr. Revaluation A/c; Cr. Machinery A/c by ₹1,20,000.

(*ix*) Dr. Revaluation A/c; Cr. *X*'s Capital A/c by ₹8,000.

Q. 41. *A* and *B* were in partnership sharing profits and losses in the ratio of 3 : 1. On Ist April, 2022 they admit *C* as a partner on the following terms :

(*a*) That *C* brings ₹1,00,000 as his capital and ₹50,000 for goodwill, half of which to be withdrawn by *A* and *B*.

(*b*) That the value of land and buildings to be appreciated by 15 per cent and that of stocks and machinery & fixtures to be reduced by 7 and 5 per cent respectively.

(*c*) That provision for doubtful debts be made at 5 per cent.

(*d*) That ₹15,000 be provided for an unforeseen liability.

(*e*) That *C* to be given 1/5th share and the profit sharing ratio between *A* and *B* to remain the same.

(*f*) That ₹11,000 is to be received as commission, hence to be accounted for.

The Balance Sheet of the old partnership as at 31st March, 2022 stood as :

Liabilities		₹	*Assets*	₹
Sundry Creditors		3,50,000	Cash in Hand	40,000
Capital Accounts :			Book Debts	2,00,000
A	4,00,000		Stock	1,80,000
B	2,00,000	6,00,000	Machinery & Fixtures	2,00,000
			Land & Building	3,30,000
		9,50,000		9,50,000

Give necessary Journal entries, ledger accounts and the balance sheet of the newly constituted firm.

[**Ans.** Profit on revaluation ₹12,900; Capital accounts *A* ₹4,28,425, *B* ₹2,09,475, *C* ₹1,00,000, Cash Balance ₹1,65,000 and Balance Sheet total ₹11,02,900.]

Hints 1. Entry for unforeseen liability :

Revaluation A/c	Dr.	15,000	
To Unforeseen liability A/c			15,000

Unforeseen liability will be shown on the liability side of the Balance Sheet.

2. Entry for Commission :

Accrued Commission A/c	Dr.	11,000	
To Revaluation A/c			11,000

Accrued Commission will be shown on the assets side of the Balance Sheet.

Reserves and Accumulated Profits

Q. 42. Khushi and Sukhi are partners in a firm sharing profits in the ratio of 5 : 4. On April 1, 2020, they admit Muskan as a new partner and the new ratio is agreed at 3 : 2 : 1. On that date there was a balance of ₹63,000 in the profit and loss account and a balance of ₹45,000 in general reserve. Record the necessary journal entries.

[**Ans.** Profit & Loss balance and General Reserve will be credited to old partners in old ratio.]

Q. 43. *A* and *B* were partners in a firm sharing profits in the ratio of 7 : 3. On 1-3-2020, they admitted *C* as a new partner for $\frac{1}{6}$th share in the profits of the firm. They fixed the new profit sharing ratio as 3 : 2 : 1. The P & L A/c on the date of admission showed a balance of ₹20,000 (Cr.). The firm also had a reserve of ₹1,50,000. *C* is to bring ₹40,000 as premium for his share of goodwill.

Showing your calculations clearly, pass necessary journal entries to record the above transactions.

[**Ans.** (*i*) P & L A/c and Reserve A/c will be debited and old partners will be credited in their old ratio. (*ii*) *A* sacrifices $\frac{6}{30}$ whereas *B* gains $\frac{1}{30}$ and *C* gains $\frac{5}{30}$. Hence Premium for Goodwill A/c will be debited by ₹40,000 and *B*'s Capital A/c will be debited by ₹8,000 and *A*'s Capital A/c will be credited by ₹48,000.]

Workmen Compensation Reserve

Q. 44. *X* and *Y* are partners in a firm. On 1st April, 2022, they admitted *Z* as a partner and new profit sharing ratio is agreed at 3 : 2 : 1. Their Balance Sheet disclosed 'Workmen Compensation Reserve' amounting to ₹1,00,000 on this date. Show the accounting treatment, if

(*i*) Claim for Workmen Compensation is estimated at ₹1,20,000.

(*ii*) Claim for Workmen Compensation is estimated at ₹90,000.

[**Ans.**

In Case (*i*) Revaluation loss of ₹20,000 debited to *X* and *Y* in equal proportion.

In Case (*ii*) Capital Accounts of *X* and *Y* credited by ₹5,000 each.]

Q. 45. *A*, *B* and *C* are partners sharing profits in 2 : 2 : 1. On 1st April, 2022, they admitted *Z* for 1/4th share. On the date of admission, the following items appeared in their Balance Sheet :

	₹
General Reserve	1,50,000
Workmen Compensation Reserve	40,000
Profit & Loss A/c (Cr.)	60,000
Advertisement Suspense A/c (Dr.)	25,000

Pass necessary journal entries.

[**Ans.** (*i*) Capital Accounts of *A*, *B* and *C* will be credited in the ratio of 2 : 2 : 1 from the amount of General Reserve, Workmen Compensation Reserve and Profit & Loss.

(*ii*) Capital Account of *A*, *B* and *C* will be debited in the ratio of 2 : 2 : 1 from the amount of Advertisement Suspense.]

Q. 46. *P* and *Q* were partners sharing profits in the ratio of 2 : 1. On 1st April, 2022, they admitted *R* as a new partner and the new profit sharing ratio of *P*, *Q* and *R* is agreed at 3 : 1 : 1. *R* brought in ₹2,00,000 as his capital and ₹60,000 as his share of premium for goodwill.

On the date of R's admission, the Balance Sheet of P and Q showed a credit balance of ₹45,000 in Profit and Loss A/c and Workmen Compensation Reserve of ₹80,000. It was agreed that there was a claim of Workmen Compensation for ₹50,000.

Pass necessary jouranl entries on R's admission.

[**Ans.** (*i*) Surplus Workmen Compensation Reserve ₹30,000 credited to P and Q in 2 : 1. (*ii*) Premium for Goodwill credited to P and Q in 1 : 2.

Investment Fluctuation Reserve

Q. 47. A and B sharing profits and losses in the ratio of 3 : 2 decide to admit C for 1/3rd share. On this date, their Balance Sheet disclosed the following items :

	₹
Investments Fluctuation Reserve	40,000
Investments (at cost)	3,00,000

Show the accounting treatment in the following cases :

Case (*i*) If the market value of investments is ₹2,90,000
Case (*ii*) If the market value of investments is ₹2,45,000
Case (*iii*) If the market value of investments is ₹3,00,000
Case (*iv*) If the market value of investments is ₹3,25,000

[**Ans.**
Case (*i*) Capital Accounts of A and B credited by ₹30,000 in 3 : 2.
Case (*ii*) Capital Accounts of A and B debited by ₹15,000 in 3 : 2.
Case (*iii*) Capital Accounts of A and B credited by ₹40,000 in 3 : 2.
Case (*iv*) Capital Accounts of A and B credited by ₹40,000 + ₹25,000 in 3 : 2]

Q. 48. Charu and Deepika were partners sharing profits in the ratio of 3 : 2. They admitted Esha, as a new partner and the new ratio is agreed at 4 : 3 : 2. On the date of Esha's admission, the Balance Sheet of Charu and Deepika disclosed General Reserve ₹1,20,000; Dr. balance in Profit & Loss Account ₹40,000; Investments ₹2,00,000 and Investment Fluctuation Reserve ₹60,000.

The following was agreed upon Eshas' admission :

(*i*) Esha will bring ₹3,00,000 as her Capital and her share of goodwill premium in cash.

(*ii*) Goodwill of the firm be valued ₹1,80,000.

(*iii*) The market value of investments was ₹2,30,000.

Pass the necessary journal entries.

[**Ans.** (*i*) Investment Fluctuation Reserve ₹60,000 and profit on revaluation ₹30,000 Credited to Charu and Deepika in 3 : 2. (*ii*) Premium for Goodwill Credited to Charu and Deepika in 7 : 3.]

Q. 49. A, B and C were partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1. Their Balance Sheet as at 31st March, 2022 was as follows :

Liabilities	₹	*Assets*	₹
Creditors	20,000	Cash & Bank	30,000
Bills Payable	5,000	Debtors	60,000

General Reserve	40,000	Stock	1,50,000
Workmen Compensation Reserve	35,000	Investments (Market Value	
Investment Fluctuation Reserve	10,000	₹32,000)	40,000
Capital Accounts :		Plant & Machinery	2,60,000
A 2,00,000		Profit & Loss Account	20,000
B 1,50,000			
C 1,00,000	4,50,000		
	5,60,000		5,60,000

They admit *D* into partnership for $\frac{1}{4}$th share on 1st April, 2022. Give necessary journal entries to adjust the accumulated profits and losses.

[**Ans.** Accumulated profits credited to *A*, *B* and *C* ₹30,800, ₹30,800 and ₹15,400 respectively. Accumulated loss debited to *A*, *B* and *C* ₹8,000, ₹8,000 and ₹4,000 respectively.]

Q. 50. Vimal and Nirmal are partners sharing profits in the ratio of 3 : 2. Following was the position of their business as at 31st March, 2022 :

Liabilities	₹	*Assets*	₹
Sundry Creditors	20,000	Cash	14,000
Capital Accounts :		Debtors	18,000
Vimal	60,000	Plant & Machinery	50,000
Nirmal	32,000	Stock	40,000
Profit & Loss A/c	20,000	Goodwill	10,000
	1,32,000		1,32,000

On 1st April, 2022, Kailash agrees to join the business on the following terms and conditions :

(*i*) He will introduce ₹40,000 as his capital and pay ₹20,000 to the existing partners for his share of goodwill.

(*ii*) The new profit sharing ratio will be 2 : 1 : 1 respectively for Vimal, Nirmal and Kailash.

(*iii*) A revaluation of assets will be made by reducing plant and machinery to ₹35,000 and stock by 10%. Provision of ₹1,000 is to be created for bad and doubtful debts.

Pass journal entries for the above arrangements and give the balance sheet of the newly constituted firm. Also specify the sacrificing ratio.

[**Ans.** Sacrifice Ratio 2 : 3; Loss on revaluation ₹20,000; Capital Accounts Vimal ₹62,000; Nirmal and Kailash ₹40,000 each; Cash Balance ₹74,000; Balance Sheet total ₹1,62,000.]

Q. 51. *X* and *Y* share profits in the ratio of 5 : 3. Their balance sheet as at 31st March, 2020, was as follows :

Liabilities	₹	*Assets*	₹
Creditors	15,000	Cash at Bank	5,000

Provident Fund	10,000	Sundry Debtors	20,000	
Workmen's Compensation Reserve	5,800	*Less* : Provision	600	19,400
		Stock		25,000
		Fixed Assets		80,000
Capitals :		Profit & Loss A/c		2,400
X	70,000			
Y	31,000			
	1,31,800			1,31,800

They admit *Z* into partnership on 1st April, 2020 with 1/8th share in profits. *Z* brings ₹20,000 as his capital and ₹12,000 for goodwill in cash. *Z* acquires his share entirely from *X*. Following revaluations are also made :

1. Provident fund is to be increased by ₹5,000.
2. Debtors are all good. Therefore, no provision is required on debtors.
3. Stock includes ₹3,000 for obsolete items.
4. Creditors are to be paid ₹1,000 more.
5. Fixed Assets are to be revalued at ₹70,000.

Prepare Journal entries, necessary accounts and new balance sheet. Also calculate the new profit sharing ratio.

[**Ans.** Loss on Revaluation ₹18,400; Capitals *X* ₹72,625; *Y* ₹25,375; *Z* ₹20,000; B/S total ₹1,49,000. New Ratio 4 : 3 : 1.]

Hint : Workmen's Compensation Reserve will be divided between the old partners.

Q. 52. *A* and *B* were partners with capitals of ₹15,00,000 and ₹20,00,000. They shared profits in the ratio of 2 : 3. On 1st April, 2020, they admitted *C* as a new partner and the new profit sharing ratio will be 3 : 3 : 4. *C* brings ₹20,00,000 as his capital.

Their assets apart from cash consisted of the following :

Fixed Assets ₹20,00,000; Stock ₹15,00,000 and Debtors ₹5,00,000. On that date Creditors were ₹4,00,000 and General Reserve ₹3,00,000.

Following revaluations were made :

(*i*) There was a liability for workmen compensation amounting to ₹50,000.

(*ii*) ₹20,000 of debtors are bad and a provision of 5% was to be created for doubtful debts.

(*iii*) Expenses debited to the Profit & Loss Account includes a sum of ₹14,000 paid for *A*'s personal expenses.

(*iv*) Stock includes ₹40,000 for obsolete items.

(*v*) Fixed assets are to be revalued at ₹18,00,000.

Goodwill of the firm is valued at ₹4,00,000 and *C* brings his share of goodwill in cash.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet of the new firm.

[**Ans.** Loss on Revaluation ₹3,20,000; Capital A/cs A ₹15,18,000; *B* ₹21,08,000 and *C* ₹20,00,000; B/S Total ₹60,76,000. Cash Balance ₹23,60,000.]

Hint : In Point (*iii*) ₹14,000 will be debited to *A*'s Capital A/c and Credited to Revaluation A/c.

Q. 53. *X* and *Y* are partners. They admit *Z* as a partner and new profit sharing ratio is agreed at 3 : 2 : 1. *Z* brings in Capital of ₹1,50,000 and ₹40,000 as premium for goodwill in Cash.

Their Balance Sheet was as follows :

Liabilities		₹	*Assets*		₹
Creditors		40,000	Cash and Bank		44,000
Capital Accounts :			Debtors	2,00,000	
X	4,00,000		*Less* : Provision	14,000	1,86,000
Y	2,50,000	6,50,000	Stock		2,50,000
Current Accounts :			Machinery		1,20,000
X	30,000		Building		2,00,000
Y	10,000	40,000			
Workmen Compensation Reserve		70,000			
		8,00,000			8,00,000

The assets and liabilities are revalued as under :

(*i*) Provision for Doubtful Debts is found in excess by ₹4,000.

(*ii*) Building was found under valued by 20% and Machinery overvalued by 20%.

(*iii*) Part of the stock which had been included at a cost of ₹10,000 had been badly damaged in storage and could only expect to realise ₹2,000.

(*iv*) Creditors were written off ₹6,000.

Pass necessary journal entries.

[**Ans.** Profit on Revaluation ₹32,000 be credited to *X* and *Y* in equal proportion.]

Hint : No. (*ii*) Dr. Building A/c and Cr. Revaluation A/c by ₹50,000
Dr. Revaluation A/c and Cr. Machinery A/c by ₹20,000

No. (*iii*) Dr. Revaluation A/c and Cr. Stock A/c by ₹8,000.

Q. 54. *X, Y* and *Z* are equal partners with capitals of ₹1,50,000, ₹1,75,000 and ₹2,00,000 respectively. They agree to admit *W* into equal partnership upon payment in cash of ₹1,50,000 for one-fourth share of the goodwill and ₹1,80,000 as his capital, both sums to remain in the business. The liabilities of the old firm amount to ₹3,00,000 and the assets apart from cash, consist of Motors ₹1,20,000; Furniture ₹40,000; Stock ₹2,65,000; Debtors ₹3,78,000.

The Motors and Furniture were revalued at ₹95,000 and ₹38,000 respectively.

Draft Journal entries necessary to give effect to the above arrangement and show the initial Balance Sheet of the new firm.

[**Ans.** Loss on revaluation ₹27,000; Capital Accounts : *X* ₹1,91,000; *Y* ₹2,16,000; *Z* ₹2,41,000 and *W* ₹1,80,000. B/S Total ₹11,28,000.]

Hint. First of all, a balance sheet will be prepared to calculate the missing figure of cash. It will be ₹22,000.

Q. 55. Gopal and Govind are partners sharing profits and losses in the ratio of 60 : 40. The firm's Balance Sheet as at 31.3.2020 was as follows :

Liabilities	₹	Assets	₹
Capital Accounts :		Fixed Assets	3,00,000
Gopal	1,20,000	Investments	50,000
Govind	80,000	Current Assets	2,00,000
Long-term Loan	2,00,000	Loans and Advances	1,00,000
Current Liabilities	2,50,000		
	6,50,000		6,50,000

Due to financial difficulties, they have decided to admit Guru as a partner in the firm from 1.4.2020 on the following terms :

Guru will be entitled to 40% of the profits.

Guru will bring in cash ₹1,00,000 as capital. It is agreed that Goodwill of the firm will be valued at 2 years' purchase of 3 years' normal average profits of the firm and Guru will bring in cash his share of Goodwill. It was also decided that the partners will not withdraw their share of goodwill nor will the goodwill appear in the books of account.

The profits of the previous three years were as follows :

For the year ended 31.3.2018 profit ₹20,000 (including insurance claim received ₹40,000).

For the year ended 31.3.2019 loss ₹80,000 (including voluntary retirement compensation paid ₹1,10,000).

For the year ended 31.3.2020 profit ₹1,05,000 (including profit of ₹25,000 on the sale of assets).

It was decided to revalue the assets on 31.3.2020 as follows :

Fixed Assets (net)	₹4,00,000
Investments	Nil
Current Assets	₹1,80,000
Loans and Advances	₹1,00,000

The new profit sharing ratio after the admission of Guru was 35 : 25 : 40.

Pass Journal entries on admission, show goodwill calculation and prepare Revaluation Account, partners' Capital Accounts, and Balance Sheet as on 1.4.2020 after the admission of Guru.

[**Ans.** Profit on Revaluation ₹30,000; Premium for Goodwill paid by Guru ₹24,000; Sacrifice Ratio 5 : 3; Capital Accounts : Gopal ₹1,53,000; Govind ₹1,01,000 and Guru ₹1,00,000; B/S Total ₹8,04,000.]

Q. 56. *A* and *B* are in partnership sharing profits and losses in the ratio of 3 : 1. Their Balance Sheet as at 31st Jan., 2020 was as follows :

Liabilities		₹	Assets	₹
Capital Accounts :			Cash at Bank	34,000
A	4,50,000		Sundry Debtors	1,66,000
B	2,00,000	6,50,000	Stock	2,60,000
Sundry Creditors		30,000	Fixed Assets	2,20,000
		6,80,000		6,80,000

As from 1st February, 2020 they agree to admit C as a partner. Share of A, B and C in the new firm will be 3 : 2 : 1 respectively. C to contribute ₹1,20,000 as his capital and ₹30,000 as his share of goodwill.

The value of the fixed assets of the firm will be increased by 10% before the admission of C.

Pass entries and prepare the opening balance sheet of the firm.

[**Ans.** Profit on Revaluation ₹22,000; Capital Accounts A ₹5,11,500; B ₹1,90,500 and C ₹1,20,000; total of B/S ₹8,52,000.]

Hint. A sacrifices $\frac{3}{12}$ and B gains $\frac{1}{12}$. Amount of compensation for goodwill to be made by B to A ₹15,000.

Q. 57. Gautam and Rahul are partners in a firm, sharing profits and losses in the ratio of 2 : 3. Their Balance Sheet as at 31st March, 2014, was as follows :

BALANCE SHEET *as at 31st March, 2014*

Liabilities		₹	*Assets*		₹
Sundry Creditors		5,000	Goodwill		10,000
Bills Payable		15,000	Furniture		25,000
General Reserve		10,000	Stock		15,000
Capital A/cs :			Sundry Debtors	12,000	
Gautam	30,000		*Less* : Provision for		
Rahul	40,000	70,000	Doubtful Debts	2,000	10,000
			Cash in hand		40,000
		1,00,000			1,00,000

Karim was to be taken as a partner with effect from 1st April, 2014, on the following terms :

(*a*) The new profit sharing ratio of Gautam, Rahul and Karim would be 5 : 3 : 2.

(*b*) Provision for Doubtful Debts would be raised to 20% of debtors.

(*c*) Karim would bring in cash, his share of capital of ₹40,000 and his share of goodwill valued at ₹10,000.

(*d*) Gautam would take over the furniture at ₹22,000.

You are required to :

(*i*) Pass journal entries at the time of Karim's admission.

(*ii*) Prepare the Balance Sheet of the reconstituted firm. *(ISC, 2015)*

[**Ans.** Loss on Revaluation ₹3,400; Capital A/cs : Gautam ₹1,640; Rahul ₹52,960 and Karim ₹40,000; B/S Total ₹1,14,600.]

Hint. Gautam gains $\frac{1}{10}$ share and Rahul sacrifices $\frac{3}{10}$ share; Amount of compensation for goodwill to be made by Gautam to Rahul ₹5,000.

Q. 58. P, Q and R were in partnership sharing profit in the proportions of 2 : 2 : 1. Their Balance Sheet as at 31st March, 2020 was as follows :

Liabilities	₹	*Assets*	₹
Creditors	80,000	Building	4,10,000

Capitals :	P	3,00,000		Machinery		1,50,000
	Q	2,80,000		Debtors	1,20,000	
	R	1,60,000	7,40,000	*Less* : Provision	8,000	1,12,000
				Stock		1,18,000
				Cash and Bank		30,000
			8,20,000			8,20,000

They admit *S* into partnership, who brings in ₹2,00,000 as his capital and a further ₹40,000 for his share of goodwill. He was given $\frac{1}{5}$th share of profits, the old partners sharing the balance in the proportions of 5 : 3 : 2.

Building is to be appreciated by 20% and Machinery is to be depreciated by 10%. Sundry Debtors are worth ₹1,10,000. A liability of ₹5,000 for outstanding expenses has been omitted to be recorded in the books.

You are required to pass journal entries and prepare the opening balance sheet of the new firm.

[**Ans.** Profit on Revaluation ₹60,000; Capital Accounts : *P* ₹3,24,000; *Q* ₹3,36,000; *R* ₹1,80,000 and *S* ₹2,00,000. Total of B/S ₹11,25,000. Sacrifice made by *Q* and *R* in the ratio of 4 : 1.]

Q. 59. *A* and *B* are in partnership sharing profits and losses in the ratio of 3 : 2. On 1st April, 2022, they admitted *C* into partnership. He paid ₹50,000 as his capital but nothing for Goodwill which was valued at ₹40,000 for the time. He acquired 1/5th share in the profits, equally from both partners. It was also decided that:

(*i*) Land and Building be written off by ₹20,000;

(*ii*) Stock be written down by ₹3,200.

(*iii*) A provision of ₹1,000 be created for doubtful debts; and

(*iv*) An amount of ₹1,200, included in Sundry Creditors, be written off as it is no longer payable.

The Balance Sheet of *A* and *B* on 31st March, 2022 was as under :

BALANCE SHEET *as at 31st March, 2022*

Liabilities		₹	*Assets*	₹
Capital Accounts :			Goodwill	10,000
A	86,000		Land and Building	60,000
B	64,000	1,50,000	Plant and Machinery	70,000
General Reserve		20,000	Stock	36,000
Sundry Creditors		31,200	Sundry Debtors	20,000
			Cash at Bank	4,000
			Cash in Hand	1,200
		2,01,200		2,01,200

Prepare Revaluation Account, Partners' Capital Accounts and new Balance Sheet of the firm.

[**Ans.** Loss on Revaluation ₹23,000; *C*'s Current A/c (Dr.) ₹8,000; Capital A/cs : *A* ₹82,200 ; *B* ₹62,800; *C* ₹50,000; B/S total ₹2,25,000.]

Hints :

1. Goodwill already appearing in the books at ₹10,000 will be written off by old partners in their old ratio.
2. *C*'s Current A/c will be debited by his share of goodwill (*i.e.*, ₹8,000) and Capital Accounts of old partners will be credited in their sacrificing ratio *i.e.*, 1 : 1.

Q. 60. *A*, *B* and *C* are partners in a firm, sharing profits and losses in the ratio of 5 : 3 : 2. They admit *D* into the firm on 1st April, 2020, when their balance sheet was as follows :

Liabilities	₹	*Assets*		₹
Partner's Capitals :		Land and Building		2,00,000
A	3,00,000	Plant and Machinery		1,50,000
B	1,50,000	Furniture		30,000
General Reserve	40,000	Stock		70,000
Sundry Creditors	52,000	Debtors	60,000	
		Less : Provision for doubtful Debts	1,200	58,800
		Cash at Bank		13,200
		C's Capital : Overdrawn		20,000
	5,42,000			5,42,000

The following terms were agreed upon :

(*i*) The new profit sharing ratio should be 4 : 3 : 1 : 2.

(*ii*) Goodwill of the firm is to be valued at 4 year's purchase of the average super-profits of the last three years. Average profits of the last three years are ₹60,000, while the normal profits that can be earned with the capital employed are ₹36,000.

(*iii*) *D* will bring in ₹1,00,000 as capital.

(*iv*) *D* could bring in only $\frac{1}{3}$rd of his share of goodwill in cash.

(*v*) Plant and machinery is to be valued at ₹1,20,000; Provision for doubtful debts is to be maintained at 5%; value of Land and Building has appreciated by 25%; furniture has depreciated by 10%.

(*vi*) An unprovided contingent liability of ₹4,000 for damages has matured for payment.

Prepare necessary journal entries, Capital Accounts and the opening Balance Sheet of the new firm.

[**Ans.** Profit on Revaluation ₹11,200; *D*'s share of goodwill ₹19,200; *D*'s Current A/c (Dr.) ₹12,800; Balance of Capital Accounts : *A* ₹3,35,200; *B* ₹1,65,360; *C* ₹160 (Dr.) and *D* ₹1,00,000. Balance Sheet Total ₹6,56,560.]

Hint : Premium for Goodwill A/c will be debited by ₹6,400 and Current Account of *D* will be debited by ₹12,800 and Capital Accounts of *A* and *C* will be credited by ₹9,600 each.

Q. 61. *A* and *B* are partners in a firm sharing profits and losses in the ratio of 3 : 2. On 31st March, 2020, their Balance Sheet was as under :

Liabilities	₹	*Assets*	₹
Creditors	1,20,000	Bank	30,000

Outstanding Expenses		30,000	Investments	1,50,000
General Reserve		1,50,000	Debtors	1,25,000
Capitals A/cs :			Stock	1,50,000
A	6,00,000		Premises	8,00,000
B	4,00,000	10,00,000	Advertisement Suspense	45,000
		13,00,000		13,00,000

On the above date *C* is admitted as a partner for 3/7th share which he takes 2/7th from *A* and 1/7th from *B*. He brings ₹2,00,000 as premium out of his share of ₹2,40,000. *C* brings ₹6,00,000 as his capital. Following terms are agreed upon :

(*i*) Premises be depreciated by 10%.

(*ii*) Accrued income ₹15,000 is to be taken into account.

(*iii*) Investments are to be increased by ₹2,00,000 and stock is to be increased to ₹2,00,000.

(*iv*) A liability of ₹10,000 included in creditors is not likely to arise.

(*v*) There is an unrecorded asset worth ₹50,000.

Prepare Revaluation A/c, Capital A/cs and the opening Balance Sheet. Also calculate the new profit sharing ratios.

[**Ans.** Profit on Revaluation ₹2,45,000; Capital A/cs *A* ₹9,70,000; *B* ₹6,20,000 and *C* ₹6,00,000. *C*'s Current A/c shown in assets ₹40,000; B/S Total ₹23,30,000. New Profit Sharing Ratio 11 : 9 : 15.]

Hidden Goodwill :

Q. 62 (A). Madhu and Neha were partners in a firm sharing profits and losses in the ratio of 3 : 5. Their fixed capitals were ₹4,00,000 and ₹6,00,000 respectively. On 1.1.2016, Tina was admitted as a new partner for $\frac{1}{4}$th share in the profits. Tina acquired her share of profit from Neha. Tina brought ₹4,00,000 as her capital which was to be kept fixed like the capitals of Madhu and Neha. Calculate the goodwill of the firm on Tina's admission and the new profit sharing ratio of Madhu, Neha and Tina. Also, pass necessary journal entry for the treatment of goodwill on Tina's admission considering that Tina did not bring her share of goodwill premium in cash.

(C.B.S.E. 2017, Outside Delhi)

[**Ans.** Hidden Goodwill ₹2,00,000; Debit Tina's Current A/c and Credit Neha's Current A/c by ₹50,000.]

Q. 62 (B). *X* and *Y* are partners with capital of ₹13,00,000 and ₹20,00,000. They share profits in the ratio of 1 : 2. They admit *Z* as a partner with 1/5th share in the profits of the firm. *Z* brings in ₹12,00,000 as his share of capital. The Profit and Loss Account showed a credit balance of ₹6,00,000 as on the date of admission of *Z*. Give the necessary Journal entries to record the goodwill.

[**Ans.** Hidden Goodwill ₹9,00,000.]

Hint : Balance of P & L will be credited to the Capital Accounts of *X* and *Y* and hidden goodwill will be calculated thereafter.

Q. 63. Asin and Shreya are partners in a firm. They admit Ajay as a new partner with 1/5th share in the profits of the firm. Ajay brings ₹5,00,000 as his share of capital.

The value of the total assets of the firm was ₹15,00,000 and outside liabilities were valued at ₹5,00,000 on that date. Give the necessary Journal entry to record goodwill at the time of Ajay's admission. Also show your workings.

[**Ans.** Hidden Goodwill ₹10,00,000; Ajay's Current Account will be debited by ₹2,00,000 and Capital Accounts of Asin and Shreya will be credited by ₹1,00,000 each.]

Q. 64. *A, B* and *C* were partners in a firm sharing profits in the ratio of 2 : 1 : 1. Their respective capitals were *A* ₹3,00,000; *B* ₹2,00,000 and *C* ₹1,80,000. On 1st April, 2022 they admitted *D* as a new partner. *D* brought ₹2,00,000 for his capital and necessary amount for his share of goodwill premium. The new profit sharing ratio between *A, B, C* and *D* will be 1 : 2 : 1 : 1.

Pass necessary journal entries for the above transactions in the books of the firm on *D*'s admission.

[**Ans.** Hidden Goodwill ₹1,20,000; Entry for Premium for Goodwill :

Premium for Goodwill A/c	Dr.	24,000	
B's Capital A/c	Dr.	18,000	
To *A*'s Capital A/c			36,000
To C's Capital A/c			6,000

Q. 65. Following figures have been extracted from the books of *X* and *Y* who share profit and losses in the ratio of 7 : 3.

	₹
X's Capital	3,00,000
Y's Capital	1,50,000
Reserve	1,60,000
Profit & Loss Account	40,000
Advertisement Expenditure	10,000

On this date, they admit *Z* for $\frac{1}{5}$th share and the new profit sharing ratio is agreed at 3 : 1 : 1. *Z* brings in ₹3,00,000 as his Capital. Pass journal entry for recording goodwill.

[**Ans.** Hidden Goodwill ₹5,60,000; *Z*'s Current A/c will be debited by ₹1,12,000 and *X* and *Y*'s Capital A/cs will be credited by ₹56,000 each. Sacrifice Ratio 1 : 1.]

Q. 66. Following is the Balance Sheet of *X* and *Y* who share profits and losses in the ratio of 3 : 2 as at 31st March, 2020 :

Liabilities		₹	*Assets*	₹
Sundry Creditors		80,000	Cash at Bank	20,000
Reserve		1,00,000	Debtors	70,000
Profit & Loss Account		40,000	Stock	1,80,000
Capital Accounts :			Machinery	3,50,000
X	2,70,000		Goodwill	30,000
Y	1,60,000	4,30,000		
		6,50,000		6,50,000

On 1st April 2020, *Z* is admitted as a new partner. *X* surrenders $\frac{1}{3}$rd of his share

and *Y* surrenders $\frac{1}{4}$th of his share in favour of *Z*. *Z* brings in ₹3,60,000 for his share of Capital. Pass journal entries for recording goodwill.

[**Ans.** Hidden Goodwill ₹3,00,000; *Z*'s Current A/c will be debited by ₹90,000 and *X* and *Y*'s Capital A/cs will be Credited by ₹60,000 and ₹30,000 respectively. Sacrifice Ratio 2 : 1; *Z*'s share in profits $\frac{3}{10}$]

Q. 67. *A, B* and *C* are partners sharing profits and losses in the ratio of 6 : 3 : 1. Their respective capitals are *A* ₹5,00,000; *B* ₹4,00,000 and *C* ₹2,00,000. They decide to admit *D* into partnership and the new profit sharing ratio is agreed at 3 : 3 : 3 : 1.

D brings ₹1,50,000 as his capital and his share of goodwill in cash. At the time of *D*'s admission :

(*a*) The firm had a Workmen Compensation Reserve of ₹1,00,000 against which there was a claim of ₹1,20,000.

(*b*) Advertisement Suspense A/c (Dr.) balance appeared in their books at ₹30,000.

(*c*) Contingency Reserve appeared at ₹60,000.

You are required to prepare necessary journal entries.

[**Ans.** Hidden Goodwill ₹2,40,000.
Entry for Premium for Goodwill :

Premium for Goodwill A/c	Dr.	24,000	
C's Capital A/c	Dr.	48,000	
To *A*'s Capital A/c			72,000]

Q. 68. Rajesh and Ravi are partners sharing profits in the ratio of 3 : 2. Their Balance Sheet stood as under as at 31st March, 2022.

BALANCE SHEET

Liabilities		₹	*Assets*		₹
Creditors		3,85,000	Cash		20,000
Outstanding liabilities		40,000	Stock		1,50,000
Capitals :			Prepaid Insurance		15,000
Rajesh	2,90,000		Debtors	94,000	
Ravi	1,50,000	4,40,000	*Less* : Provision	4,000	90,000
			Machinery		1,90,000
			Buildings		3,50,000
			Furniture		50,000
		8,65,000			8,65,000

Raman is admitted as a new partner introducing a capital of ₹1,60,000. The new profit-sharing ratio is decided as 5 : 3 : 2. Raman is unable to bring in any cash for Goodwill. So, it is decided to value the goodwill on the basis of Raman's share in the profits and the capital contributed by him. Following revaluations are made :

(*i*) Stock to depreciate 5%.

(*ii*) Provision for doubtful debts is to be ₹5,000.

(*iii*) Furniture to depreciate 10%.

(*iv*) Buildings are valued at ₹4,00,000.

Show the necessary Ledger Accounts and the Balance Sheet of the new firm.

[**Ans.** Profit on Revaluation ₹36,500; Raman's Current A/c (Dr.) ₹32,700; Capital Accounts : Rajesh ₹3,28,250; Ravi ₹1,80,950; Raman ₹1,60,000. B/S Total ₹10,94,200.]

Hints: (*i*) Hidden Goodwill ₹1,63,500.

(*ii*) Raman's Current A/c will be debited by his share of Goodwill *i.e.*, ₹32,700 and Capital Accounts of Rajesh and Ravi will be credited in their sacrificing ratio *i.e.*, equally.

Adjustment of Capital Accounts

New Partner's Capital not given

Q. 69. Nem and Khem sharing profits in the ratio of 3 : 2 admit Prem as a partner with 1/3 share in profits. He had to contribute proportionate capital. They had following financial position :

Liabilities	₹	*Assets*	₹
Creditors	40,000	Cash at Bank	5,000
Reserve Fund	50,000	Debtors	60,000
Capitals :		Stock	35,000
Nem	50,000	Plant and Machinery	80,000
Khem	40,000		
	1,80,000		1,80,000

They agreed to admit Prem as a partner on the following terms :

(1) Plant and Machinery to be reduced by 10%.

(2) Stock to be increased by ₹3,000.

(3) Bad debts provision was to be created at 5%.

(4) Accrued incomes not appearing in the books ₹900.

(5) Prem was to introduce ₹20,000 as premium for goodwill for 1/3rd share of the future profits of the firm.

Prepare Profit and Loss Adjustment Account, Capital Accounts and Balance Sheet of the new firm. Also calculate new profit sharing ratio.

[**Ans.** Loss on Revaluation ₹7,100; Capital Accounts : Nem ₹87,740; Khem ₹65,160 and Prem ₹76,450; Bank Balance ₹1,01,450; and Balance Sheet Total ₹2,69,350. New profit sharing ratio 6 : 4 : 5.]

Hint : Calculation of Prem's Capital :

Combined Capital of Nem and Khem for $\frac{2}{3}$ share of Profits

$= 87{,}740 + 65{,}160 =$ ₹1,52,900

Therefore, the total Capital of the new firm will be $= 1{,}52{,}900 \times \frac{3}{2} =$ ₹2,29,350

Prem's Capital for $\frac{1}{3}$ rd share $= 2{,}29{,}350 \times \frac{1}{3} =$ ₹76,450

Q. 70. Following is the Balance Sheet of *A* and *B* who are sharing profits in the ratio of 2 : 3.

Liabilities		Amount	Assets	Amount
		₹		₹
Trade Payables		2,60,000	Goodwill	50,000
Outstanding Expenses		40,000	Plant & Machinery	5,20,000
Capitals :			Stock	4,60,000
A	5,00,000		Debtors	3,80,000
B	7,00,000	12,00,000	Bank Balance	66,000
			Deferred Revenue Expenditure	24,000
		15,00,000		15,00,000

C is admitted into partnership on the following terms :

(*i*) *A* gives $\frac{1}{4}$th of his share and *B* gives $\frac{1}{5}$th of his share to *C*.

(*ii*) Goodwill is agreed to be valued at 2.5 year's purchase of the average normal profit of past three years, which were :

2018	Profit	₹ 40,000	(including profit on sale of assets ₹50,000)
2019	Loss	₹ 90,000	(including loss by fire ₹2,00,000)
2020	Profit	₹2,00,000	(including insurance claim received ₹60,000)

(*iii*) *C* does not bring his share of goodwill in Cash.

(*iv*) *C* brings in capital proportionate to his share of profit in the firm.

Pass necessary journal entries. Also calculate new profit sharing ratio.

[**Ans.** *C*'s Capital ₹3,30,000. New Profit Sharing Ratio 15 : 24 : 11.]

Hint. *C*'s Current A/c will be debited by his share of goodwill ₹44,000 and Capital Accounts of *A* and *B* will be credited in their sacrificing ratio i.e., 5 : 6.

Q. 71. Mohan and Mahesh were partners in a firm sharing profits in the ratio of 3 : 2. On 1st April, 2012 they admitted Nusrat as a partner in the firm. The Balance Sheet of Mohan and Mahesh on that date was as under :

BALANCE SHEET OF MOHAN AND MAHESH
as at 1st April, 2012

Liabilities		₹	Assets	₹
Creditors		2,10,000	Cash in Hand	1,40,000
Workmen's Compensation Fund		2,50,000	Debtors	1,60,000
General Reserve		1,60,000	Stock	1,20,000
Capitals :			Machinery	1,00,000
Mohan	1,00,000		Building	2,80,000
Mahesh	80,000	1,80,000		
		8,00,000		8,00,000

It was agreed that :

(*i*) The value of Building is to be appreciated to ₹3,80,000.

(*ii*) Stock is undervalued by 25%.

(*iii*) The liability of workmen's compensation fund was determined at ₹2,30,000.

(*iv*) Nusrat brought in her share of goodwill ₹1,00,000 in cash.

(*v*) Nusrat was to bring further cash as would make her capital equal to 20% of the combined capital of Mohan and Mahesh after above revaluation and adjustments are carried out.

(*vi*) The future profit sharing ratio will be Mohan 2/5th, Mahesh 2/5th, Nusrat 1/5th.

Prepare Revaluation Account, Partner's Capital Accounts and Balance Sheet of the new firm. Also show clearly the calculation of capital brought by Nusrat.

[**Ans.** Profit on Revaluation ₹1,40,000; Capital Accounts : Mohan ₹3,92,000; Mahesh ₹2,08,000; Nusrat ₹1,20,000. B/S Total ₹11,60,000]

Hints :

(*i*) Actual Value of Stock : $1,20,000 \times \frac{100}{75} =$ ₹1,60,000

(*ii*) Whole sacrifice is made by Mohan.

Q. 72. On 31st March 2019, the Balance Sheet of *A* and *B*, who were sharing profits in the ratio of 3 : 2 was as follows :

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Sundry Creditors		2,50,000	Cash at Bank		1,30,000
Investment Fluctuation Reserve		50,000	Sundry Debtors	7,50,000	
Capitals :			*Less* : Provision	30,000	7,20,000
A	10,00,000		Stock		4,50,000
B	8,00,000	18,00,000	Investments		2,00,000
			Plant & Machinery		6,00,000
		21,00,000			21,00,000

They decide to admit *C* as a partner. *A* sacrifices $\frac{2}{15}$ from his share while *B* sacrifices $\frac{1}{6}$th of his share in favour of *C*.

The following adjustments were agreed upon :

(*i*) *C* shall bring ₹1,50,000 as his share of goodwill premium and shall bring in proportionate capital.

(*ii*) Stock was undervalued by 10% and Plant and Machinery was overvalued by 20%.

(*iii*) Market value of investments is ₹2,20,000.

(*iv*) Debtors to the extent of ₹10,000 were unrecorded.

(*v*) 5% provision for doubtful debts is required on sundry debtors.

Prepare Revaluation Account, Partner's Capital Accounts and the Balance Sheet of the reconstituted firm.

[**Ans.** Loss on Revaluation ₹28,000; Capital Accounts *A* ₹11,13,200; *B* ₹8,58,800 and *C* ₹4,93,000; Balance Sheet Total ₹27,15,000.]

Hints :

(*i*) Investments Fluctuation Reserve A/c	Dr.	50,000	
To *A*'s Capital A/c			30,000
To *B*'s Capital A/c			20,000
(*ii*) Investments A/c	Dr.	20,000	
To Revaluation A/c			20,000

(*iii*) Actual Value of Stock ₹5,00,000

(*iv*) Actual Value of Plant & Machinery ₹5,00,000

(*v*) Sacrificing Ratio 2 : 1

Q. 73. *P* and *Q* are partners sharing profits in 3 : 1. *R* is admitted and the partners decide to share the future profits in the ratio of 2 : 1 : 1. The Balance Sheet of *P* and *Q* as at 31st March, 2022 was as under :

Liabilities		₹	*Assets*	₹
Creditors		30,000	Bank	15,000
Profit & Loss Account		60,000	Debtors	60,000
Capital A/cs :			Stock	1,50,000
P	3,50,000		Prepaid Expenses	20,000
Q	2,20,000	5,70,000	Plant & Machinery	1,40,000
			Premises	2,75,000
		6,60,000		6,60,000

It was decided that :

(*i*) Part of the stock which has been included at a cost of ₹8,000 had been badly damaged in storage and could realise only ₹2,000.

(*ii*) A bill for ₹7,000 for electric charges has been omitted to be recorded.

(*iii*) Plant & Machinery was found overvalued by ₹20,000. Premises be appreciated to ₹3,00,000.

(*iv*) Prepaid expenses be brought down to 40%.

(*v*) *R*'s share of goodwill is valued at ₹20,000 but he is unable to bring it in cash.

(*vi*) *R* brings in capital proportionate to his share of profit in the firm.

Prepare Revaluation A/c, Capital A/cs and the opening Balance Sheet.

[**Ans.** Loss on Revaluation ₹20,000; Capital A/cs *P* ₹4,00,000; *Q* ₹2,30,000; and *R* ₹2,10,000; Balance Sheet Total ₹8,77,000]

Hints :

(1) Entry for Stock :

Revaluation A/c	Dr.	6,000	
To Stock A/c			6,000

(2) Since *R* is unable to bring in goodwill in cash, his Current A/c will be debited instead of his Capital A/c with the amount of goodwill. Following entry will be passed for it :

R's Current A/c	Dr.	20,000	
To *P*'s Capital A/c			20,000

Q. 74. X and Y are partners in a firm. They share profits and losses in the ratio of 2 : 1. Their Balance Sheet as at 31st March, 2020 stood as under :

Liabilities	₹	*Assets*		₹
Capitals :		Plant and Machinery		1,75,000
X	1,40,000	Furniture and Fixture		65,000
Y	1,00,000	Stock		35,000
Workmen Compensation Reserve	40,000	Bills Receivable		12,000
Creditors	1,50,000	Debtors	1,10,000	
Bills Payable	10,000	*Less* : Provision for Doubtful Debts	7,000	1,03,000
		Cash & Bank Balance		50,000
	4,40,000			4,40,000

Z is admitted in the partnership. X surrenders $\frac{2}{5}$th of his share and Y surrenders $\frac{1}{5}$th of his share in favour of Z. The following information is given about the firm :

(*i*) Plant and Machinery be reduced by ₹35,000 and furniture and fixture be reduced to ₹58,500.

(*ii*) Provision for bad and doubtful debts is to be increased by ₹3,000.

(*iii*) Actual liability for workmen compensation claim is ₹16,000.

(*iv*) A liability of ₹2,500 included in creditors is not likely to arise.

(*v*) Z's share of goodwill is valued at ₹40,000 but he is unable to bring it in cash.

(*vi*) Z is to bring in capital proportionate to his share of profit after all adjustments.

Prepare Revaluation Account, Capital Accounts and Balance Sheet after Z's admission. Also calculate the new profit sharing ratio.

[**Ans.** Loss on Revaluation ₹42,000; Capital Accounts : X ₹1,60,000; Y ₹1,02,000 and Z ₹1,31,000; Cash & Bank Balance ₹1,81,000; Z's Current A/c (Dr.) 40,000; Balance Sheet Total ₹5,66,500; Sacrificing Ratio 4 : 1; New Ratio 6 : 4 : 5.]

Hints : (1) Workmen Compensation Reserve is appearing at ₹40,000, whereas, the actual liability is ₹16,000. Hence, ₹16,000 will be shown in liabilities and ₹24,000 will be transferred to the credit side of Capital Accounts of old partners in their old ratio.

(2) Since Z is unable to bring in his share of goodwill in cash his Current A/c will be debited instead of his Capital A/c from his share of goodwill.

Q. 75. Given below is the Balance Sheet of S as at 31st March, 2020 :

Liabilities	₹	*Assets*		₹
Capital	2,00,000	Building		1,50,000
Sundry Creditors	75,000	Furniture and Fittings		50,000
		Bills Receivable		10,000
		Sundry Debtors	25,000	
		Less : Provision for Doubtful Debts	5,000	20,000
		Cash at Bank		45,000
	2,75,000			2,75,000

T was admitted as a partner for a half share of profits on the following conditions:

(1) Building to be appreciated by 20%.

(2) Furniture and fittings to be written down to ₹45,000.

(3) Bills receivable not to be taken over by the new partnership.

(4) Provision for doubtful debts was found to be in excess by ₹3,000.

(5) A liability of ₹2,000 included in creditors was not likely to arise.

(6) There is an additional liability of ₹5,000 being outstanding salary payable to employees of the firm.

T is to bring ₹30,000 as premium for goodwill and further cash to make his capital equal to $\frac{3}{5}$th of *S*'s capital.

Pass journal entries and prepare the opening Balance Sheet of the partnership.

[**Ans.** Profit on Revaluation ₹25,000; Capital Accounts *S* ₹2,45,000 and *T* ₹1,47,000; Bank Balance ₹2,22,000 and Balance Sheet Total ₹4,70,000.]

Adjustment of Capital Accounts
On the Basis of New Partner's Capital

Q. 76. *A* and *B* are partners sharing profits in the ratio of 2 : 1. Following items appeared in their Balance Sheet as at 31st March, 2022 :

A's Capital ₹48,000; *B*'s Capital ₹30,000; Creditors ₹15,000; Bank balance ₹5,000; Debtors ₹20,000; Machinery ₹36,000; Stock ₹44,000.

They admit *C* into partnership on 1st April, 2022 with 1/6th share in profits, which he acquires equally from *A* and *B*. He brings in ₹20,000 as his capital and ₹18,000 as goodwill in cash.

Following revaluations were made :

I. 5% provision be made for doubtful debts on Debtors and a provision of 2% be made on Debtors and Creditors for discount.

II. ₹1,000 are prepaid for insurance.

III. ₹5,000 are outstanding for salaries.

IV. ₹1,480 for accrued income are to be shown in the books.

V. Investments for ₹6,000 have been omitted to be recorded in the books.

A and *B* decide to have their capitals in proportion to their share in profits, based on *C*'s share. Any excess of capital was to be withdrawn and deficit to be paid in Cash.

Prepare the partner's capital accounts and give the new balance sheet of the firm.

[**Ans.** Profit on Revaluation ₹2,400; Capitals *A* ₹70,000; *B* ₹30,000 and *C* ₹20,000; Bank balance ₹32,600; B/S total ₹1,39,700; New profit sharing ratio 7 : 3 : 2. Cash brought in by *A* ₹3,400; Cash withdrawn by *B* ₹13,800.]

Hint : The following balance sheet will be prepared first of all, to calculate the missing figure *i.e.*, profit or loss :

Liabilities	₹	*Assets*	₹
A's Capital	48,000	Bank Balance	5,000

B's Capital	30,000	Debtors	20,000
Creditors	15,000	Machinery	36,000
P & L A/c (Balancing figure)	12,000	Stock	44,000
	1,05,000		1,05,000

Q. 77. *A, B* and *C* are partners in a firm sharing profits in the ratio of 5 : 3 : 2. *D* is admitted into the firm for 1/4 share in profits, which he gets as 1/8 from *A* and 1/8 from *B*. The total capital of the firm is agreed upon as ₹3,20,000 and *D* is to bring in cash equivalent to 1/4 of this amount as his capital. The capitals of other partners are also to be adjusted in the ratio of their respective shares in profits. The capitals of *A, B* and *C* after all adjustments are ₹1,00,000, ₹75,000 and ₹60,000 respectively. Calculate the new capitals of *A, B* and *C*, and record the necessary journal entries.

[**Ans.** New Ratio 15 : 7 : 8 : 10; Cash brought in by *A* ₹20,000 and *C* ₹4,000; Cash withdrawn by *B* ₹19,000.]

Q. 78. *A* and *B* are partners sharing profits in the ratio of 5 : 3. *C* was admitted for $\frac{1}{4}$th share in profits. *C* acquires this share as $\frac{3}{16}$ from *A* and $\frac{1}{4}$th of his share from *B*. *C* brings in ₹1,00,000 as his capital.

At the time of *C*'s admission :

(*i*) The firm's goodwill was valued at ₹2,40,000.

(*ii*) General Reserve was ₹40,000.

(*iii*) Profit on revaluation of assets and liabilities was ₹24,000.

Before any adjustments were made, the Capitals of *A* and *B* were ₹1,20,000 and ₹70,000 respectively.

It is decided that after *C*'s admission, the Capitals of *A* and *B* be adjusted on the basis of *C*'s Capital, any excess or shortfall to be adjusted by withdrawing or bringing in Cash by the old partners. You are required to pass necessary journal entries on *C*'s admission.

[**Ans.** Capitals after adjustment for goodwill, general reserve and profit on revaluation : *A* ₹2,05,000 and *B* ₹1,09,000; Final Capitals *A* ₹1,75,000 and *B* ₹1,25,000; *A* withdraws ₹30,000 and *B* brings in ₹16,000.

Hint. Sacrificing Ratio 3 : 1; New Ratio 7 : 5 : 4.

Q. 79. *A* and *B* are partners sharing profits in the proportion of 3 : 2. Their Balance Sheet as at 31st March, 2022 was as follows :

Liabilities		₹	*Assets*		₹
Sundry Creditors		63,000	Cash at Bank		5,000
Outstanding Salaries		4,000	Sundry Debtors	30,000	
General Reserve		10,000	*Less* : Provision	1,000	29,000
Capitals :	*A*	50,000	Stock		40,000
	B	30,000	Trade Marks		8,000
			Building		75,000
		1,57,000			1,57,000

They agree to admit C as a new partner on the following terms :

(1) C will be given 2/9th share of profit and he will bring ₹50,000 for his share of capital and goodwill.

(2) Goodwill of the firm will be calculated at $2\frac{1}{2}$ year's purchase of the average super profits of last four years. Profits of the last four years are ₹40,000; ₹40,000; ₹55,000 and ₹65,000 respectively. Normal profits that can be earned with the capital employed are ₹14,000.

(3) Half the amount of goodwill is withdrawn by old partners.

(4) 15% of the general reserve is to remain as a provision against doubtful debts.

(5) Outstanding salaries be increased to ₹16,000, Stock is overvalued by 25% and Building is undervalued by 25%. Trade Marks be written off by 50%.

(6) New profit sharing ratio of partners will be 4 : 3 : 2 and the capital accounts of A and B will be adjusted on the basis of C's capital by bringing in or withdrawing cash, as the case may be.

Prepare necessary accounts and the opening balance sheet of the firm.

[**Ans.** Profit on Revaluation ₹1,000; Capitals A ₹60,000; B ₹45,000; and C ₹30,000; Bank Balance ₹50,500; A withdraws ₹2,700 and B brings in ₹8,200; Balance Sheet Total ₹2,14,000. Sacrifice Ratio 7 : 3. Premium for goodwill brought in by C ₹20,000]

Hints : (*i*) Actual Value of Stock $= 40{,}000 \times \frac{100}{125} =$ ₹32,000

(*ii*) Actual Value of Building $= 75{,}000 \times \frac{100}{75} =$ ₹1,00,000

Q. 80. X and Y were partners sharing profits and losses in the ratio of 2 : 1 respectively. The following was their balance sheet as at 31st March, 2020 :

Liabilities	₹	*Assets*	₹
Creditors	80,000	Machinery	5,00,000
Outstanding Expenses	20,000	Stock	4,00,000
X's Capital	7,20,000	Debtors	3,50,000
Y's Capital	4,80,000	Prepaid Expenses	10,000
		Bank Balance	40,000
	13,00,000		13,00,000

On 1st April, 2020, Z was admitted to the firm on the following terms :

(*i*) Z would provide ₹5,00,000 as his capital and pay ₹30,000 as goodwill for his one-third share in future profits.

(*ii*) X, Y and Z would share profits equally.

(*iii*) Assets are to be revalued as :
Stock at 20% less; Debtors ₹3,20,000; Machinery ₹4,50,000; Prepaid Expenses — Nil.

(*iv*) Outstanding Expenses were estimated at ₹40,000.

(*v*) A credit purchase of goods for ₹30,000 had been omitted from the books although the goods have been included in stock.

(*vi*) Creditors include a contingent liability of ₹50,000, which has been decided by the court at ₹40,000.

(*vii*) Capital accounts of old partners would be adjusted in the profit sharing ratio on the basis of *Z*'s capital by bringing in or taking out cash.

Pass necessary journal entries and prepare partners' capital accounts and balance sheet of the new firm.

[**Ans.** Loss on Revaluation ₹2,10,000; Final Capitals ₹5,00,000 each; *X* withdraws ₹1,10,000 and *Y* brings in ₹90,000; Bank balance ₹5,50,000; B/S Total ₹16,40,000.]

Hints : (*i*) Credit purchase will be shown on the Debit of Revaluation A/c and will also be added in Creditors.

(*ii*) ₹10,000 in respect of contingent liability will be shown on the Cr. of Revaluation A/c and will also be deducted from Creditors.

Q. 81. Amit and Sumit are partners sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as at 31st March, 2022 is given below :

Liabilities		₹	*Assets*		₹
Capital A/cs :			Land and Building		3,20,000
Amit	1,76,000		Investments		
Sumit	2,54,000	4,30,000	(Market Value ₹55,000)		50,000
Loan from Puneet		3,00,000	Debtors	3,00,000	
General Reserve		30,000	*Less :* Provision for		
Employee's Provident Fund		10,000	Doubtful Debts	10,000	2,90,000
Creditors		50,000	Stock		1,10,000
			Cash at Bank		50,000
		8,20,000			8,20,000

They decided to admit Puneet as a new partner from 1st April, 2022 on the following terms :

(*i*) Amit will give 1/3rd of his share and Sumit will give 1/4th of his share to Puneet.

(*ii*) Puneet's Loan Account will be converted into his Capital.

(*iii*) The Goodwill of the firm is valued at ₹3,00,000. Puneet will bring in his share of Goodwill in cash and the same was immediately withdrawn by the partners.

(*iv*) Land and Building was found undervalued by ₹1,00,000.

(*v*) Stock was found overvalued by ₹60,000.

(*vi*) Provision for Doubtful Debts will be made equal to 5% of Debtors.

(*vii*) Investments are to be valued at their market price.

It was decided that the total capital of the firm after admission of new partner would be ₹10,00,000. Capital Accounts of Partners will be readjusted on the basis of their profit-sharing ratio and excess or deficiency will be adjusted in cash.

Prepare (*i*) Revaluation Account; (*ii*) Partner's Capital Accounts; and (*iii*) Balance Sheet of the firm after admission of new partner.

[**Ans.** Profit on Revaluation ₹40,000; Capital Accounts : Amit ₹4,00,000, Sumit ₹3,00,000 and Puneet ₹3,00,000; Amit brings in ₹1,82,000 and Sumit brings in ₹18,000; Balance Sheet Total ₹10,60,000; Sacrificing Ratio 2 : 1.]

Q. 82. *P* and *Q* are partners sharing profits and losses in the ratio of 60 : 40. The firm's Balance Sheet as at 31.3.2020 was as follows :

Liabilities	₹	*Assets*	₹
Creditors	45,000	Land and Building	1,50,000
Outstanding Liabilities	15,000	Investments	30,000
Profit & Loss A/c	20,000	Stock	1,20,000
Capitals :		Debtors	60,000
P	1,80,000	Bank	20,000
Q	1,20,000		
	3,80,000		3,80,000

R was admitted as a partner from 1.4.2020 on the following terms :

(*i*) *R* will be entitled to 40% of the profits. The new profit sharing ratio of *P*, *Q* and *R* will be 35 : 25 : 40.

(*ii*) *R* will bring in cash ₹2,00,000 as capital. It is agreed that goodwill shall be valued on the basis of capitalisation at 8% of the normal average profits of the last three years, which were as follows :

For the year ended 31.3.2018 Loss ₹80,000 (including a loss of ₹60,000 due to theft).

For the year ended 31.3.2019 Profit ₹76,000 (including a speculative profit of ₹1,00,000).

For the year ended 31.3.2020 Profit ₹1,40,000

(*iii*) Since *R* is unable to bring his share of goodwill in cash it is decided that his current account will be debited from his share of goodwill.

(*iv*) A reduction of ₹5,000 should be made from the stock in respect of old and unsalable items.

(*v*) There is an additional liability of ₹10,000 being outstanding salary payable to employees of the firm. This liability is not included in the outstanding liabilities stated in the above balance sheet.

(*vi*) Investments are worthless.

(*vii*) A bill for ₹2,000 for electric charges has been omitted and is to be accounted for.

(*viii*) Capitals are to be adjusted according to profit sharing ratio taking *R*'s Capital as base, any excess or deficiency to be adjusted in cash.

Prepare journal entries, capital accounts and the opening Balance Sheet of the new firm.

[**Ans.** Loss on Revaluation ₹47,000; Capital Accounts : *P* ₹1,75,000; *Q* ₹1,25,000 and *R* ₹2,00,000; *P* withdraws ₹8,800 and *Q* brings in ₹3,800. Bank balance ₹2,15,000; Balance Sheet Total ₹5,72,000.]

Hint : *R*'s Current A/c will be debited by his share of Goodwill ₹32,000 and *P* and *Q* will be credited in their sacrificing ratio of 5 : 3.

Q. 83 (A). *A* and *B* were partners in a firm sharing profits in 3 : 2 ratio. On 1-4-2020 they admitted *C* as a new partner and the new profit sharing ratio is agreed at 5 : 3 : 2. Their Balance Sheet as at that date was as follows :

Liabilities		₹	*Assets*		₹
Creditors		1,10,000	Plant & Machinery		3,00,000
Capitals :			Stock		1,80,000
A	3,50,000		Debtors	1,40,000	
B	1,80,000	5,30,000	*Less* : Provision for		
General Reserve		80,000	Bad Debts	5,000	1,35,000
			Investments		60,000
			Bank		25,000
			Advertisement Suspense Account		20,000
		7,20,000			7,20,000

C will bring ₹1,60,000 as his capital and the other terms agreed upon were :

(*i*) *C*'s share of goodwill is estimated at ₹60,000 but he fails to bring his share of goodwill in cash.

(*ii*) Stock is valued at ₹2,00,000 and provision for doubtful debts is to be raised to ₹7,000.

(*iii*) An amount of ₹12,000 has been paid for insurance premium during the year out of which ₹2,000 is related to the period after 31st March, 2016.

(*iv*) An accrued income of ₹10,000 is to be recorded in the books.

(*v*) A takes over the investments at ₹75,000.

(*vi*) It was found that the creditors included a sum of ₹15,000 which is not to be paid. But there is a liability for workmen compensation amounting to ₹40,000.

(*vii*) Capital Accounts of partners to be adjusted on the basis of *C*'s contribution of capital to the firm and excess or shortfall to be transferred to Current Accounts.

Prepare Revaluation Account, Capital Accounts and the New Balance Sheet of the firm.

[**Ans.** Profit on Revaluation ₹20,000; Capital Accounts *A* ₹4,00,000; *B* ₹2,40,000 and *C* ₹1,60,000; *A*'s Current A/c ₹47,000 (Dr.); *B*'s Current A/c ₹2,000 (Cr.); B/S Total ₹9,37,000.

Hint : *C*'s share of goodwill will be debited to his Current Account.

Q. 83 (B). Angad and Vivek are partners in a firm sharing profits and losses in the ratio of 3 : 2. Their balance sheet as at 1st January, 2005 was as follows :

BALANCE SHEET

Liabilities	₹	*Assets*	₹
General Reserve	10,000	Debtors	18,000

Creditors		15,000	Stock	20,000
Capital Accounts :			Furniture	10,000
Angad	30,000		Plant	30,000
Vivek	25,000	55,000	Cash	2,000
		80,000		80,000

Gopal is admitted as partner on the above date on the following terms :

(*i*) He will pay ₹10,000 as goodwill for one-fourth share in the profits of the firm.

(*ii*) The assets are to be valued as under :
Plant at ₹32,000; Stock at ₹18,000

(*iii*) A provision for bad debts at 5% on debtors has to be created.

(*iv*) It was found that the creditors included a sum of ₹1,400 which was not to be paid. There is an unrecorded liability for ₹5,000 which is to be recorded in the books.

(*v*) Gopal was to introduce ₹20,000 as capital and the capitals of other partners were to be adjusted in the new profit sharing ratio. For this purpose, current accounts were to be opened.

Prepare :

(*a*) The Capital Accounts of Angad, Vivek and Gopal.

(*b*) The Balance Sheet of the new firm. (*I.S.C. 2007*)

[**Ans.** Loss on Revaluation ₹4,500; New Ratio 9 : 6 : 5. Capital A/cs : Angad ₹36,000; Vivek ₹24,000; Gopal ₹20,000; Current A/cs : Angad ₹3,300 (Cr); Vivek ₹7,200 (Cr); Cash Balance ₹32,000; Balance Sheet total ₹1,09,100.]

Q. 84. *A* and *B* are partners in a firm sharing profits in the ratio of 3 : 2. On March 31, 2022, their Balance Sheet showed a general reserve of ₹54,000. On that date they decided to admit *C* as a new partner. The new profit sharing ratio between *A, B* and *C* will be 4 : 3 : 2. Record the necessary journal entry in the books of the firm under the following circumstances :

(*i*) When they want to distribute the general reserve.

(*ii*) When they don't want to distribute the general reserve and prefer to record an adjustment entry for the same.

[**Ans.**

(*i*) General Reserve A/c	Dr.	₹54,000	
To *A*'s Capital A/c			₹32,400
To *B*'s Capital A/c			₹21,600
(*ii*) *C*'s Current A/c	Dr.	₹12,000	
To *A*'s Capital A/c			₹ 8,400
To *B*'s Capital A/c			₹ 3,600]

Q. 85. On 1st April 2022, *A* and *B* sharing profits in the ratio of 7 : 5 admit *C* for $\frac{1}{5}$th share in profits which he acquires equally from *A* and *B*. On this date, Profit & Loss

Account showed a credit balance of ₹45,000. Partners do not want to distribute the profit but prefer to record it by passing an adjustment entry. You are required to give the journal entry.

[**Ans.** *C*'s Current A/c will be debited by ₹9,000 and Capital A/cs of *A* and *B* will be credited by ₹4,500 each.]

Q. 86. *A* and *B* are partners sharing profits in the ratio of 2 : 3. They admitted *C* as a new partner. *A* surrendered $\frac{1}{5}$th of his share and *B* $\frac{1}{3}$rd of his share in favour of *C*. On this date, Profit & Loss Account shows a Dr. Balance of ₹75,000 and Advertisement Suspense A/c ₹25,000.

Partners do not want to distribute the accumulated losses. You are required to give the adjusting entry.

[**Ans.**	*A*'s Capital A/c	Dr.	8,000	
	B's Capital A/c	Dr.	20,000	
	To *C*'s Current A/c			28,000]

Q. 87. Rani and Seeta were partners sharing profits in the ratio of 3 : 1. They admitted Mona as a new partner from 1st April, 2022. New profit sharing ratio is agreed at 3 : 2 : 1. On this date, their Balance Sheet disclosed the following items :

BALANCE SHEET (an extract)

Liabilities	₹	*Assets*	₹
General Reserve	5,00,000	Profit and Loss (Dr.)	1,10,000
		Advertisement Suspense Account	30,000

Partners decided to record the effect of the above items without affecting their book values. Pass the necessary adjusting entry.

[**Ans.**	Seeta's Capital A/c	Dr.	30,000	
	Mona's Current A/c	Dr.	60,000	
	To Rani's Capital A/c			90,000

Q. 88. Amrita and Barkha are partners sharing profits in the ratio of 5 : 3. On 1st March, 2022 they admit Fiza as a new partner and the new ratio is agreed at 3 : 1 : 1. On this date their books show 'Workmen Compensation Reserve' of ₹1,60,000. Partners do not want to alter the value of any item of Balance Sheet and want to record the effect of admission by passing an adjustment entry. You are required to pass the adjustment entry under following alternative cases.

(*i*) When there is no claim for Workmen Compensation.
(*ii*) When claim for Workmen Compensation is estimated at ₹ 40,000
(*iii*) When claim for Workmen Compensation is estimated at ₹1,60,000
(*iv*) When claim for Workmen Compensation is estimated at ₹3,00,000

[**Ans.**
(*i*) Dr. Fiza by ₹32,000 and Cr. Amrita by ₹4,000 and Barkha by ₹28,000;
(*ii*) Dr. Fiza by ₹24,000 and Cr. Amrita by ₹3,000 and Barkha by ₹21,000;
(*iii*) No Entry
(*iv*) Dr. Amrita by ₹3,500 and Barkha by ₹24,500 and Credit Fiza by ₹28,000]

Q. 89. *A* and *B* are partners sharing profits and losses in the ratio of 3 : 2. They admit *C* as a new partner from 1st April, 2022. *A* surrenders $\frac{1}{3}$rd of his share and *B* surrenders $\frac{1}{5}$th from his share in favour of *C*. Following balances appeared in their Balance Sheets as at that date :

BALANCE SHEET
as at 1st April, 2022

Liabilities	₹	*Assets*	₹
Investment Fluctuation Reserve	60,000	Investments (at Cost)	4,50,000

Partners decide that book value of any item in the Balance Sheet is not to be altered but prefer to record the change in profit sharing ratio by an adjustment entry. Show the adjustment entry under the following alternative cases :

Case 1 If there is no other information
Case 2 If the market value of investments is ₹4,35,000
Case 3 If the market value of investments is ₹3,50,000
Case 4 If the market value of investments is ₹5,00,000

[**Ans.** Sacrifice Ratio 1 : 1; *C*'s Share $\frac{2}{5}$.

Case (*i*) Dr. *C*'s Current A/c by ₹24,000 and Cr. *A*'s Capital A/c and *B*'s Capital A/c by ₹12,000 each;

Case (*ii*) Dr. *C*'s Current A/c by ₹18,000 and Cr. *A*'s Capital A/c and *B*'s Capital A/c by ₹9,000 each;

Case (*iii*) Dr. *A*'s Capital A/c and *B*'s Capital A/c by ₹8,000 each and Cr. *C*'s Current A/c by ₹16,000;

Case (*iv*) Dr. *C*'s Current A/c by ₹44,000 and Cr. *A*'s Capital A/c and *B*'s Capital A/c by ₹22,000 each.

Q. 90. *A, B* and *C* are partners sharing profits and losses in the ratio of 9 : 6 : 5. Their Balance Sheet as at 31st March, 2022 was as follows :

Liabilities		₹	*Assets*	₹
Sundry Creditors		2,40,000	Land and Building	6,00,000
Profit and Loss Account		15,000	Investments	1,50,000
General Reserve		1,20,000	Stock	4,05,000
Investment Fluctuation Reserve		45,000	Sundry Debtors	3,10,000
Workmen Compensation Reserve		80,000	Cash at Bank	10,000
Capital Accounts :			Advertisement Suspense Account	25,000
A	5,00,000			
B	3,00,000			
C	2,00,000	10,00,000		
		15,00,000		15,00,000

D is admitted as a new partner for $\frac{1}{4}$th of the future profits and losses. *B* sacrifices

$\frac{1}{10}$th from his share in favour of D and rest of the sacrifice was made by A and C in the ratio of 2 : 1. Claim on account of Workmen Compensation is estimated at ₹50,000. Market value of investments was ₹1,25,000.

Partners do not want to alter the values given in the Balance Sheet but prefer to record the effect of change in profit sharing ratio by an adjustment entry. You are required to give the necessary journal entry. Also calculate new profit sharing ratio.

[**Ans.** Sacrificing Ratio 2 : 2 : 1.   New Ratio 7 : 4 : 4 : 5

D's Current A/c ($\frac{1}{4}$ of 1,60,000)	Dr.	40,000	
To A's Capital A/c ($\frac{2}{5}$ of 40,000)			16,000
To B's Capital A/c ($\frac{2}{5}$ of 40,000)			16,000
To C's Capital A/c ($\frac{1}{5}$ of 40,000)			8,000]

Q. 91. A and B are partners sharing profits in the ratio of 7 : 5. Their Balance Sheet as at 31st December, 2021 was as follows :

Liabilities		₹	*Assets*		₹
Sundry Creditors		75,000	Building		6,00,000
General Reserve		1,50,000	Stock		1,80,000
Workmen Compensation Reserve		40,000	Investments		
Investment Fluctuation Reserve		35,000	(Market Value ₹90,000)		1,00,000
Capital Accounts :			Sundry Debtors	1,50,000	
A	5,00,000		*Less :* Provision for		
B	4,00,000	9,00,000	Doubtful		
			Debts	15,000	1,35,000
			Cash at Bank		1,45,000
			Advertisement Expenditure		40,000
		12,00,000			12,00,000

They admit C as a partner. A sacrifices 1/7th of his share and B sacrifices 1/6th from his share in favour of C.

Following terms are agreed upon :

(*i*) Goodwill is valued at ₹2,40,000. C brings ₹2,00,000 as capital and his share of goodwill in cash.

(*ii*) Ravi, an old customer whose account was written off as bad has promised to pay ₹12,000 in full settlement of his account of ₹15,000.

(*iii*) Provision for doubtful debts to be reduced by ₹10,000.

(*iv*) Claim on account of Workmen Compensation is ₹25,000.

(*v*) Stock is overvalued by 20% and building is undervalued by 25%.

(*vi*) After adjusting the claim of Workmen Compensation from Workmen Compensation reserve and difference between book value and market value of investments from Investment Fluctuation Reserve, remaining balance of such

reserves alongwith all accumulated profits/losses are to appear in the Balance Sheet of the new firm.

Prepare Revaluation Account, Partner's Capital Accounts and the reconstituted Balance Sheet.

[**Ans.** Profit on Revaluation ₹1,92,000; Capital Accounts : *A* ₹6,44,500; *B* ₹5,45,000 and *C* ₹2,00,000; *C*'s Current A/c (Dr.) ₹37,500; B/S Total ₹16,79,500.]

Hints :

(*i*) Sacrifice Ratio 1 : 2; New Ratio 2 : 1 : 1.

(*ii*) Entry for promise by an old customer :

Sundry Debtors A/c	Dr.	12,000	
To Revaluation A/c			12,000

(*iii*) Adjustment to be made for Accumulated Profits/Losses :

		₹
	General Reserve	1,50,000
	Workmen Compensation Reserve	15,000
+	Investment Fluctuation Reserve	25,000
		1,90,000
(–)	Advertisement Expenditure	40,000
		1,50,000

C's Current A/c ($\frac{1}{4}$ of ₹1,50,000)	Dr.	37,500	
To *A*'s Capital A/c ($\frac{1}{3}$ of ₹37,500)			12,500
To *B*'s Capital A/c ($\frac{2}{3}$ of ₹37,500)			25,000

Q. 92. *P* and *Q* are partners sharing profits in the ratio of 3 : 2. Following is their Balance Sheet as at 31st March, 2022 :

Liabilities		₹	*Assets*		₹
Sundry Creditors		1,45,000	Land and Building		9,50,000
General Reserve		1,80,000	Stock		2,00,000
Workmen Compensation Reserve		25,000	Investments		
Investment Fluctuation Reserve		50,000	(Market Value ₹1,00,000)		1,20,000
Capital Accounts :			Sundry Debtors	3,00,000	
P	8,00,000		*Less :* Provision for		
Q	4,00,000	12,00,000	Doubtful		
			Debts	30,000	2,70,000
			Cash at Bank		10,000
			Advertisement Suspense A/c		50,000
		16,00,000			16,00,000

On 1st April, 2022, they agreed to take *R* as a partner on the following terms :

(*i*) *P* sacrifices $\frac{1}{4}$th of his share and *Q* sacrifices $\frac{1}{20}$ from his share in favour of *R*.

(*ii*) Goodwill of the firm is valued at ₹2,00,000.

(*iii*) *C* brings ₹2,50,000 as his capital but brings only 60% of his share of goodwill in cash.

(*iv*) Land and Building is undervalued by ₹50,000 and stock is overvalued by ₹40,000.

(*v*) Claim on account of Workmen Compensation is ₹40,000.

(*vi*) There is an unrecorded asset worth ₹30,000 and Provision for Doubtful Debts be reduced to ₹20,000.

(*vii*) Expenses debited in the Profit & Loss Account includes a sum of ₹25,000 paid for *P*'s personal life insurance policy.

(*viii*) General Reserve is to appear at its original figure in the Balance Sheet of the new firm.

Prepare Revaluation Account, Partner's Capital Accounts and Balance Sheet of the new firm.

[**Ans.** Profit on Revaluation ₹60,000; Capital Accounts : *P* ₹8,56,000; *Q* ₹4,35,000 and *R* ₹2,50,000; *R*'s Current A/c (Dr.) ₹52,000 (₹16,000 for Goodwill and ₹36,000 for General Reserve); Balance Sheet Total ₹19,06,000; Cash at Bank ₹2,84,000.]

Hints :

(*i*)	Sacrifice Ratio 3 : 1; New Ratio 9 : 7 : 4			
(*ii*)	Adjustment Entry for Workmen Compensation Claim :			
	Workmen Compensation Reserve A/c	Dr.	25,000	
	Revaluation A/c	Dr.	15,000	
	To Workmen Compensation Claim A/c			40,000
(*iii*)	Adjustment Entry for Investment Fluctuation Reserve :			
	Investment Fluctuation Reserve A/c	Dr.	50,000	
	To Investments A/c			20,000
	To *P*'s Capital A/c			18,000
	To *Q*'s Capital A/c			12,000
(*iv*)	Advertisement Suspense is to be debited to the Capital Accounts of *P* and *Q* in the ratio of 3 : 2.			

ADDITIONAL QUESTIONS

Q. 93. Rekha, Sunita and Teena are partners in a firm sharing profits in the ratio of 3 : 2 : 1. Samiksha joins the firm. Rekha surrenders $\frac{1}{4}$th of her share; Sunita surrenders $\frac{1}{3}$rd of her share and Teena $\frac{1}{5}$th of her share in favour of Samiksha. Find the new profit-sharing ratio. *(C.B.S.E. Sample Paper, 2017)*

[**Ans.** New Profit Sharing Ratio 135 : 80 : 48 : 97]

Q. 94. Calculate sacrificing ratios in the following cases :

(*i*) *X* and *Y* are sharing profits in the ratio of 4 : 3. *Z* joins and the new ratios are 7 : 4 : 3.

(*ii*) X and Y are sharing profits in the ratio of 7 : 5. Z joins and the new ratios are 13 : 7 : 4.

(*iii*) A and B are sharing profits in the ratio of 5 : 3. C joins and the new ratios are 4 : 2 : 1.

(*iv*) A and B are sharing profits in the ratio of 3 : 2. C joins and the new ratios are 5 : 3 : 2.

[**Ans.** (*i*) 1 : 2, (*ii*) 1 : 3, (*iii*) 3 : 5, (*iv*) 1 : 1.]

Q. 95. Calculate new ratios and sacrificing ratios in the following cases :

(*i*) A, B and C are partners sharing profits in the ratio of 4 : 3 : 2. D is admitted for 1/3rd share.

(*ii*) A, B and C are partners sharing profits in the ratio of 1/2, 1/3 and 1/6. D is admitted for 1/6th share of profits.

(*iii*) A, B and C are partners sharing profits in the ratio of 6/14, 5/14 and 3/14. D is admitted for 1/8th share of profits.

[**Ans.** (*i*) New Ratio 8 : 6 : 4 : 9; Sacrifice Ratio 4 : 3 : 2.
(*ii*) New Ratio 15 : 10 : 5 : 6; Sacrifice Ratio 3 : 2 : 1.
(*iii*) New Ratio 6 : 5 : 3 : 2; Sacrifice Ratio 6 : 5 : 3.]

Q. 96. Kabir and Farid are partners in a firm sharing profits in the ratio of 3 : 1. On 1-4-2019 they admitted Manik into partnership for 1/4th share in the profits of the firm. Manik brought his share of goodwill premium in cash. Goodwill of the firm was valued on the basis of 2 years purchase of last three years average profits. The profits of last three years were :

	₹
2016-17	90,000
2017-18	1,30,000
2018-19	86,000

During the year 2018-19 there was a loss of ₹20,000 due to fire which was not accounted for while calculating the profit.

Calculate the value of goodwill and pass the necessary journal entries for the treatment of goodwill. *(C.B.S.E. 2020, Delhi)*

[**Ans.** Premium for Goodwill brought in by Manik ₹51,000 will be Credited to Kabir and Farid in their sacrificing ratio of 3 : 1.]

Hint : Loss due to fire ₹20,000 will be ignored since it has not been considered while calculating the profit.

Q. 97. Lucy, Rahul and Sanjay are partners sharing profits and losses in the ratio of 1 : 2 : 3. Arun is admitted as a partner who brings in ₹20,000 as his capital for 1/5th share in the profit. Goodwill of the firm is to be valued at an average of the last three years profits which were ₹25,000, ₹28,000 and ₹37,000 respectively. Arun is unable to bring in cash towards his share of premium of goodwill.

Give the journal entries if goodwill already appears in the books at ₹24,000. *(I.S.C. 2010)*

[**Ans.** Arun's Current A/c will be debited by ₹6,000 and Capital Accounts of Lucy, Rahul and Sanjay will be credited in 1 : 2 : 3]

Q. 98. *A* and *B* are partners sharing profits in the ratio of 3 : 2. They admit *C* into partnership, *C* pays a premium of ₹60,000 for 1/4th share of profit. The new ratio is 3 : 3 : 2. Goodwill account appears in the books at ₹2,00,000. Give the necessary Journal entries.

[**Ans.** Goodwill of ₹2,00,000 written off by *A* and *B* in their old ratio, *i.e.*, 3 : 2. Premium for goodwill brought in by *C* will be credited to *A* and *B* in sacrificing ratio of 9 : 1.]

Q. 99. *A* and *B* are partners sharing profits in the ratio of 5 : 3. They admit *C* as a partner for 1/3rd share. His share of Goodwill is ₹32,000. Give journal entries in the following cases :

(*a*) When the amount of goodwill is paid privately.

(*b*) When the goodwill is received in cash and retained in the business.

(*c*) When the goodwill is received in cash and withdrawn by old partners.

(*d*) When *C* is unable to bring the goodwill in cash.

Hint : In case (*a*) there will be no entry for goodwill.
In case (*b*) and (*c*) Premium A/c will be debited by ₹32,000 and Capital A/cs of *A* and *B* will be credited in 5 : 3.
In case (*d*) Current A/c of *C* will be debited by ₹32,000 and Capital A/cs of *A* and *B* will be credited in 5 : 3.]

Q. 100. *A* and *B* are partners. They admit *C* as partner who pays ₹50,000 as capital. The new ratio is to be 4 : 3 : 2. The goodwill of the firm is to be based on 2 years' purchase of the average of 3 years' profits which were ₹30,000; ₹35,000 and ₹43,000. Show Journal entries, if :

(*a*) *C* pays for goodwill in cash; and

(*b*) He is unable to bring cash for goodwill.

[**Ans.** In case (*a*), Premium for goodwill ₹16,000 brought in cash divided by *A* and *B* in their sacrificing ratio 1 : 3.

In case (*b*), *C*'s Current A/c will be debited by ₹16,000 and Capital Accounts of *A* and *B* will be credited in 1 : 3.]

Q. 101. *A* and *B* are partners sharing profits in the ratio of 2 : 1. They admit *C* for 1/4th share in profits. *C* brings ₹30,000 for his capital and ₹8,000 out of his share of ₹10,000 for goodwill. Before admission goodwill appeared in books at ₹18,000. Give Journal entries to give effect to above arrangement.

Hints : 1. Goodwill of ₹18,000 written off by *A* and *B* in 2 : 1.

2. Goodwill of ₹8,000 brought in cash by *C* will be credited to Premium for Goodwill A/c.

3. Premium for Goodwill A/c will be debited by ₹8,000 and *C*'s Current A/c will be debited by ₹ 2,000 and Capital Accounts of *A* and *B* will be credited in 2 : 1.

Revaluation of Assets and Liabilities

Q. 102. *A* and *B* are partners sharing profits in the ratio of 3 : 2. Their Balance Sheet stood as under as at 31st August, 2022 :

Liabilities	₹	*Assets*	₹
Creditors	2,50,000	Bank	72,000

Outstanding Rent		10,000	Debtors	2,00,000	
			Less : Provision	12,000	1,88,000
Capital Accounts :			Stock		2,50,000
A	5,00,000		Machinery		1,50,000
B	3,00,000	8,00,000	Buildings		4,00,000
		10,60,000			10,60,000

On that date *C* is admitted as a partner. *A* sacrifices 1/3 of his share and *B* 1/4 of his share in favour of *C*. Following terms are agreed upon :

(*i*) Goodwill is valued at ₹1,50,000. *C* is to bring in his share of goodwill in cash.

(*ii*) Provision for Doubtful Debts is to be 5% of debtors.

(*iii*) Outstanding rent amounted to ₹25,000 and prepaid insurance ₹13,000.

(*iv*) Building is to be increased to ₹5,00,000 and Stock by ₹25,000.

(*v*) *C* is to contribute ₹3,50,000 as his capital.

Prepare Revaluation Account, Partner's Capital Accounts and the Balance Sheet of the new firm.

[**Ans.** Sacrifice Ratio 2 : 1. *C*'s share 3/10; Profit on Revaluation ₹1,25,000; Capital Ac/s *A* ₹6,05,000, *B* ₹3,65,000 and *C* ₹3,50,000; B/S Total ₹15,95,000.]

Q. 103. Raman and Aman were partners in a firm and were sharing profits in 3 : 1 ratio. On 31-3-2019 their balance sheet was as follows :

BALANCE SHEET OF RAMAN AND AMAN

as at 31-3-2019

Liabilities		₹	*Assets*	₹
Provision for Bad Debts		7,000	Bank	24,000
Outstanding Expenses		18,000	Bills Receivable	80,000
Bills Payable		47,000	Sundry Debtors	95,000
Sundry Creditors		1,02,000	Stock	14,000
Workmen Compensation Reserve		55,000	Furniture	70,000
Capitals :			Machinery	2,00,000
Raman	3,00,000		Land & Building	1,96,000
Aman	1,50,000	4,50,000		
		6,79,000		6,79,000

On the above date Suman was admitted as a new partner for 1/5th share in the profits on the following conditions :

(*i*) Suman will bring ₹2,00,000 as her capital and necessary amount for her share of goodwill premium. The goodwill of the firm on Suman's admission was valued at ₹1,00,000.

(*ii*) Outstanding expenses will be paid off. ₹5,000 will be written off as bad debts and a provision of 5% for bad debts on debtors was to be maintained.

(*iii*) The liability towards workmen compensation was estimated at ₹60,000.

(*iv*) Machinery was to be depreciated by ₹18,000 and Land and Building was to be depreciated by ₹54,000.

Pass necessary journal entries for the above transactions in the books of the firm.

(C.B.S.E. 2020, Punjab)

[**Ans.** Loss on Revaluation ₹79,500]

Hint : Revaluation A/c Dr. 2,500
To Provision for Doubtful Debts 2,500

Q. 104. *A* and *B* share the profits of a business in the ratio of 5 : 3. They admit *C* into the firm for a 1/4th share in the profits to be contributed equally by *A* and *B*. On the date of admission of *C*, the Balance Sheet of the firm was as follows :

Liabilities	₹	*Assets*	₹
A's Capital	3,00,000	Machinery	2,60,000
B's Capital	2,00,000	Furniture	1,60,000
Workmen's Compensation		Stock	1,20,000
Reserve	40,000	Debtors	80,000
Bank Loan	1,20,000	Bank	60,000
Creditors	20,000		
	6,80,000		6,80,000

Terms of *C*'s admission were as follows :

(*i*) *C* will bring ₹3,30,000 for his share of capital and goodwill.

(*ii*) Goodwill of the firm has been valued at 4 years' purchase of the average super profits of last three years. Average profits of the last three years are ₹2,20,000 while the normal profits that can be earned with the capital employed are ₹1,40,000.

(*iii*) Furniture is to be appreciated by ₹60,000 and the value of stock is to be reduced by ₹20,000.

Prepare Revaluation Account, Partners' Capital Accounts and the new Balance Sheet of *A*, *B* and *C*.

[**Ans.** Revaluation Profit ₹40,000; Partners' Capital Accounts : *A* ₹3,90,000; *B* ₹2,70,000 and *C* ₹2,50,000; Total of Opening Balance Sheet ₹10,50,000.]

Q. 105. *A* and *B* are partners in a firm sharing profits and losses as 5 : 3. The position of the firm as at 31st March, 2020 was as follows :

Liabilities		₹	*Assets*	₹
Capital Accounts :			Plant and Machinery	40,000
A	30,000		Stock	30,000
B	20,000	50,000	Sundry Debtors	20,000
Sundry Creditors		15,000	Bills Receivable	10,000
Bank Overdraft		42,500	Cash at Bank	7,500
		1,07,500		1,07,500

On 1st April, 2020 *C* joins them on condition that he will share 3/4th of the future profits, the balance of profits being shared by *A* and *B* as 5 : 3. He introduces ₹40,000 by way of capital and further ₹4,000 by way of premium for goodwill. He also

provides loan to the firm to pay off bank overdraft. *A* and *B* agree to depreciate Plant by 10% and to raise a reserve against Sundry Debtors @ 5%.

You are asked to journalise the entries in the books of the firm and show the resultant Balance Sheet. How will the partners share future profits?

[**Ans.** Revaluation Loss ₹5,000; Capitals : *A* ₹29,375; *B* ₹19,625; *C* ₹40,000; Balance Sheet Total ₹1,46,500. New Ratio 5 : 3 : 24.]

Hint : Instead of Bank Overdraft, *C*'s Loan A/c will be shown on the liabilities side of the opening Balance Sheet. Following entry will be passed for it :

Bank Overdraft A/c	Dr.	42,500	
To *C*'s Loan A/c			42,500

Q. 106. Rohit and Bal sharing profits in the ratio of 5 : 3 had the following Balance Sheet as at March 31, 2019 :

BALANCE SHEET

Liabilities	₹	*Assets*	₹
Creditors	1,00,000	Goodwill	1,50,000
Bills Payable	40,000	Building	1,70,000
General Reserve	1,40,000	Plant	1,35,000
Capital Accounts :		Furniture	20,000
Rohit	4,00,000	Debtors	1,65,000
Bal	2,00,000	Bills Receivables	75,000
		Stock	1,10,000
		Bank	55,000
	8,80,000		8,80,000

On April 1st, 2019, they decided to admit Khosla into the partnership giving him 1/5th share. He brings in ₹2,50,000 as his share of capital. The partners decide to revalue the Assets as follows :

Goodwill ₹2,50,000; Plant ₹1,25,000; Debtors ₹1,55,000; Stock ₹1,62,500; Building ₹2,00,000; Furniture ₹10,000; Bills Receivable ₹62,500.

You are required to show the journal entries and prepare the Revaluation A/c.

[**Ans.** Profit on Revaluation ₹40,000.]

Hint : Entries for Goodwill :

(*i*)	Rohit's Capital A/c	Dr.	93,750	
	Bal's Capital A/c	Dr.	56,250	
	To Goodwill A/c			1,50,000
	(Goodwill written off in old ratio of 5 : 3)			
(*ii*)	Khosla's Current A/c	Dr.	50,000	
	To Rohit's Capital A/c			31,250
	To Bal's Capital A/c			18,750
	(Capital Accounts of old partners credited in their sacrificing ratio of 5 : 3 for Khosla's share of goodwill on his admission.)			

Q. 107. *A* and *B* are partners in a firm. Their Balance Sheet as at 31st March, 2020 was as follows :

Liabilities	₹	Assets	₹
Capital :		Cash	10,000
A	50,000	Sundry Debtors	80,000
B	60,000	Stock	20,000
Creditors	15,000	Fixed Assets	38,600
Outstanding Expenses	3,000	P & L A/c	4,000
Insurance Fund	7,000		
Provident Fund	1,000		
Employees Saving Fund	5,000		
Workmen Profit Sharing Fund	2,000		
Workmen Compensation Reserve	5,600		
Provision for Doubtful Debts	4,000		
	1,52,600		1,52,600

C was taken into partnership as from 1st April, 2020 on following terms for 1/6 share :

1. *C* will bring ₹40,000 as his capital.
2. Goodwill is valued at ₹12,000 and admitting partner is unable to bring his share of goodwill in cash.
3. Claim on account of Workmen's Compensation is ₹3,000.
4. Creditors are to be paid ₹2,000 more.
5. 2% Provision for Discount on Debtors is required.
6. The share of *A* in new firm will be $1\frac{1}{2}$ times of *B*.

Prepare Revaluation A/c, Capital Accounts and Balance Sheet.

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	Particulars		₹
To Creditors	2,000	By Loss transferred to :		
To Provision for Discount(1)	1,520	*A*'s Capital A/c	1,760	
		B's Capital A/c	1,760	3,520
	3,520			3,520

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	A	B	C	Particulars	A	B	C
	₹	₹	₹		₹	₹	₹
To P & L A/c	2,000	2,000		By Bal. b/d	50,000	60,000	
To Revaluation	1,760	1,760		By Insurance Fund	3,500	3,500	
To Balance c/d	51,040	63,040	40,000	By Workmen Compensation Reserve	1,300	1,300	

				By C's Current A/c ($\frac{1}{6}$ of 12,000)		2,000	
				By Cash			40,000
	54,800	66,800	40,000		54,800	66,800	40,000

BALANCE SHEET

as at 1st April, 2020

Liabilities		₹	*Assets*	₹
Capitals :			Cash	50,000
A	51,040		Sundry Debtors	80,000
B	63,040		Stock	20,000
C	40,000	1,54,080	Fixed Assets	38,600
Creditors		17,000	C's Current A/c	2,000
Outstanding Exp.		3,000		
Provident Fund		1,000		
Employee's Saving Fund		5,000		
Workmen Profit Sharing Fund		2,000		
Provision for Workmen Compensation Claim		3,000		
Provision for Doubtful Debts		4,000		
Provision for Discount on Debtors		1,520		
		1,90,600		1,90,600

Note : (1) Provision for Discount will be 2% on (₹80,000 – Provision for Doubtful Debts ₹4,000)

(2) New Profit Sharing Ratio :

C is admitted for $\frac{1}{6}$th share. Balance $\frac{5}{6}$th will be shared by A and B in the ratio of

$1\frac{1}{2} : 1$ or $3 : 2$

Hence, A's share : $\frac{5}{6} \times \frac{3}{5} = \frac{3}{6}$

B's share : $\frac{5}{6} \times \frac{2}{5} = \frac{2}{6}$

C's share : $= \frac{1}{6}$

Sacrificing Ratio :

$A = \frac{1}{2} - \frac{3}{6} = 0$

$B = \frac{1}{2} - \frac{2}{6} = \frac{1}{6}$

Hence, only B has sacrificed

Q. 108. The Balance Sheet of A and B as at 31st March, 2020 is given below :

Liabilities	₹	*Assets*	₹
A's Capital	60,000	Freehold Property	20,000

B's Capital	30,000	Furniture	6,000
General Reserve	24,000	Stock	12,000
Creditors	16,000	Debtors	80,000
		Cash	12,000
	1,30,000		1,30,000

A and *B* share profits and losses in the ratio of 2 : 1. On 1st April, 2020 they agree to admit *P* into the firm subject to the following terms and conditions :

(*a*) *P* will bring in ₹21,000 of which ₹9,000 will be treated as his share of Goodwill to be retained in the business.

(*b*) *P* will be entitled to 1/4 share of profits of the firm.

(*c*) 50% of the General Reserve is to remain as a provision for bad and doubtful debts.

(*d*) Furniture is to be depreciated by 5%.

(*e*) Stock is to be revalued at ₹10,500.

Prepare Revaluation Account, Capital Accounts and Opening Balance Sheet of the new firm.

[**Ans.** Loss on Revaluation ₹1,800; Capital Balances : *A* ₹72,800; *B* ₹36,400; *P* ₹12,000; Cash Balance ₹33,000; B/S Total ₹1,37,200.]

Hint : Entry for General Reserve will be :

General Reserve A/c	Dr.	24,000	
To Provision for bad & doubtful debts A/c			12,000
To *A*'s Capital A/c			8,000
To *B*'s Capital A/c			4,000

Q. 109. *A* and *B* are partners sharing profits and losses in the ratio of 3 : 2. On April 1, 2020, their Balance Sheet was as follows :

Liabilities		₹	*Assets*	₹
Sundry Creditors		51,000	Goodwill	15,000
Workmen Compensation Reserve		4,000	Plant	75,000
Capitals :			Patents	8,000
A	1,00,000		Stock	80,000
B	1,20,000	2,20,000	Debtors	62,000
			Cash	20,000
			Profit & Loss Account	15,000
		2,75,000		2,75,000

On this date they agree to admit *C* on the following terms :

(*i*) *C* will be entitled to 3/10 share in the profits which he acquires 1/5 from *A* and 1/10 from *B*. He will bring in ₹60,000 as his capital.

(*ii*) Goodwill of the firm was valued at ₹40,000.

(*iii*) Plant is valued at ₹60,000 and Stock at ₹70,000.

(*iv*) Claim on account of Workmen's Compensation is ₹6,000.

(*v*) Patents should be written off.

(*vi*) Investments of ₹5,000 which did not appear in the books should be duly recorded.

(*vii*) *B* is to withdraw ₹20,000 in cash.

Give journal entries and the Balance Sheet of the new firm.

[**Ans.** Loss on Revaluation ₹30,000; *C*'s Current A/c (Dr.) ₹12,000; Capitals Accounts *A* ₹72,000; *B* ₹80,000 and *C* ₹60,000; B/S Total ₹2,69,000; Sacrificing Ratio 2 : 1.]

Hints : (1) Goodwill already appearing in the assets will be written off between the old partners in their old ratio.

(2) Following entry will be passed in respect of Workmen Compensation :

Workmen Compensation Reserve A/c	Dr.	4,000	
Revaluation A/c	Dr.	2,000	
To Liability for Workmen Compensation Claim A/c			6,000

Liability for Workmen Compensation Claim will appear on the liabilities side of the Balance Sheet at ₹6,000.

Note : *C*'s Current A/c has been debited from his share of goodwill.

Q. 110. *A* and *B* were partners with fixed capitals of ₹3,70,000 each. They admitted *C* as a new partner for 1/4th share of profits. *C* brought ₹3,00,000 as his capital and the necessary amount of goodwill premium for his share of goodwill. The new profit sharing ratio will be 2 : 1 : 1.

Pass necessary journal entries for the above transactions in the books of the firm.

[**Ans.** Hidden Goodwill ₹1,60,000. Entire amount of goodwill ₹40,000 brought in by *C* will be credited to *B*'s Current A/c since he alone has sacrificed.]

Q. 111. *A*, *B* and *C* were partners in a firm sharing profits in the ratio of 2 : 1 : 2. Their respective fixed capitals were *A* ₹7,00,000; *B* ₹4,50,000 and *C* ₹6,00,000. On 31st March, 2022, they admitted Divya as a new partner for 1/5th share in the profits. Their new profit sharing ratio was 1 : 2 : 1 : 1. Divya brought ₹5,00,000 as her capital and necessary amount for her share of goodwill premium.

Pass necessary journal entries for the above transactions in the books of the firm on Divya's admission.

[**Ans.** Hidden Goodwill ₹2,50,000. Entry for premium for goodwill :

Premium for Goodwill A/c	Dr.	50,000	
B's Current A/c	Dr.	50,000	
To *A*'s Current A/c			50,000
To *C*'s Current A/c			50,000

Q. 112. David and Bimal are partners sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as at 31st March 2020, was as follows :

BALANCE SHEET

as at 31st March, 2020

Liabilities	₹	*Assets*	₹
Sundry Creditors	8,20,000	Cash	3,20,000
General Reserve	30,000	Stock	1,50,000

Capital A/cs :			Debtors	94,000	
David	1,80,000		*Less* : Provision for		
Bimal	1,20,000	3,00,000	Doubtful Debts	4,000	90,000
			Building		5,50,000
			Furniture		40,000
		11,50,000			11,50,000

They admitted Chander as a new partner on 1-4-2020 and the new profit sharing ratio became 5 : 3 : 2. Chander introduced a capital of ₹1,60,000. Chander was unable to bring any cash for goodwill and so it was decided to value the goodwill on the basis of his share in the profits and the capital contributed by him. Adjustment for the same should be made through a current account opened in the name of Chander. The following revaluations were made at the time of Chander's admission :

(*i*) Stock had been overvalued by ₹7,500 and furniture by ₹5,000.

(*ii*) Provision for doubtful debts to be increased by ₹1,000.

(*iii*) A creditor for ₹23,500 was paid off by Bimal privately for which no entry was passed in the books of the firm.

Prepare the Revaluation Account, Partner's Capital Accounts and a Balance Sheet of the new firm on the date of Chander's admission. Show your workings clearly.

[**Ans.** Loss on Revaluation ₹13,500; Chander's Current A/c (Dr.) ₹60,000; Capital Accounts : David ₹2,19,900; Bimal ₹1,80,100 and Chander ₹1,60,000; B/S total ₹13,56,500.]

Hint. Hidden Goodwill ₹3,00,000.

Calculation of the Capital Introduced by the New Partner

Q. 113. Leena and Rohit are partners in a firm sharing profits in the ratio of 3 : 2. On 31st March, 2018, their Balance Sheet was as follows :

BALANCE SHEET OF LEENA AND ROHIT

as at 31-3-2018

Liabilities		₹	*Assets*		₹
Sundry Creditors		80,000	Cash		42,000
Bills Payable		38,000	Debtors	1,32,000	
General Reserve		50,000	*Less* : Provision for		
Capital :			Doubtful Debts	2,000	1,30,000
Leena	1,60,000		Stock		1,46,000
Rohit	1,40,000	3,00,000	Plant and Machinery		1,50,000
		4,68,000			4,68,000

On the above date Manoj was admitted as a new partner for 1/5th share in the profits of the firm on the following terms :

(*i*) Manoj brought proportionate capital. He also brought his share of goodwill premium of ₹80,000 in cash.

(*ii*) 10% of the general reserve was to be transferred to provision for doubtful debts.

(*iii*) Claim on account of workmen's compensation amounted to ₹40,000.

(*iv*) Stock was overvalued by ₹16,000.

(*v*) Leena, Rohit and Manoj will share future profits in the ratio of 5 : 3 : 2.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet of the reconstituted firm. *(C.B.S.E. 2019)*

[**Ans.** Loss on Revaluation ₹56,000; Capital Accounts : Leena ₹1,93,400; Rohit ₹1,75,600 and Manoj ₹92,250; B/S Total ₹6,19,250; Sacrificing Ratio 1 : 1.]

Q. 114. On 31st March, 2019 the Balance Sheet of Madan and Mohan who share profits and losses in the ratio of 3 : 2 was as follows :

Balance Sheet of Madan and Mohan

as at 31st March, 2019

Liabilities		₹	*Assets*		₹
Creditors		28,000	Cash at Bank		10,000
General Reserve		10,000	Debtors	65,000	
Employees Provident Fund		22,000	*Less* : Provision for		
Capitals :			Doubtful Debts	5,000	60,000
Madan	60,000		Stock		33,000
Mohan	40,000	1,00,000	Patents		57,000
		1,60,000			1,60,000

They decided to admit Gopal on 1st April, 2019 for 1/5th share which Gopal acquired wholly from Mohan on the following terms :

(*i*) Gopal shall bring ₹10,000 as his share of premium for Goodwill.

(*ii*) A debtor whose dues of ₹3,000 were written off as bad debt paid ₹2,000 in full settlement.

(*iii*) A claim of ₹5,000 on account of workmen's compensation was to be provided for.

(*iv*) Patents were undervalued by ₹2,000. Stock in the books was valued 10% more than its market value.

(*v*) Gopal was to bring in capital equal to 20% of the combined capitals of Madan and Mohan after all adjustments.

Prepare Revaluation Account, Capital Accounts of the Partners and the Balance Sheet of the new firm. *(C.B.S.E. 2019, C)*

[**Ans.** Loss on Revaluation ₹4,000; Capitals : Madan ₹63,600; Mohan ₹52,400 and Gopal ₹23,200; Bank Balance ₹45,200; Balance Sheet Total ₹1,94,200.]

Q. 115. *A* and *B* are partners in a firm. They share profits and losses as 4/5th and 1/5th respectively. Below is given the Balance Sheet of the firm as at 31st March, 2020:

Liabilities		₹	*Assets*	₹
Capital Accounts :			Plant	75,000
A	1,15,000		Stock	80,000
B	35,000	1,50,000	Debtors	60,000

Sundry Creditors	65,000	Cash	25,000
Bills Payable	15,000	Goodwill	20,000
Reserve	30,000		
	2,60,000		2,60,000

C wants to join the firm from 1st April, 2020. He is willing to pay goodwill premium to partners amounting to ₹20,000. In return he will be allowed to share 1/5th of the future profits of the firm which he acquires equally from *A* and *B*. The following revaluation of the assets is agreed upon : Plant to be reduced to ₹60,000, stock to ₹65,000 and debtors to ₹50,000 (₹10,000 proved bad debts). The new partner is to introduce 50% of the adjusted capitals of the existing partners. You are required to give journal entries recording the above transactions. Give also the opening balance sheet of the new firm and new profit-sharing ratio.

[**Ans.** Loss on revaluation ₹40,000; Capital : *A* ₹1,01,000; *B* ₹39,000; and *C* ₹70,000; Balance Sheet total ₹2,90,000; New profit sharing ratio 7 : 1 : 2.]

Hint : As the new partner has brought his share of goodwill in cash, goodwill appearing in the balance sheet will be written off by the old partners in their old ratio.

Q. 116. *A* and *B* are partners in a firm sharing profit and losses in the ratio of 3 : 1. On 1st April, 2022 their position was as given below :

Liabilities		₹	*Assets*	₹
Capital Accounts :			Goodwill	20,000
A	2,00,000		Plant	1,00,000
B	80,000	2,80,000	Patents	10,000
Sundry Creditors		70,000	Stock	1,42,000
Workmen Compensation Reserve		10,000	Sundry Debtors	50,000
			Cash	18,000
			Profit & Loss Account	20,000
		3,60,000		3,60,000

They admit *C* into partnership with 1/6th share in profits upon the following terms:

(I) Goodwill is to be valued at one year's purchase of the five years' average profits which were ₹20,000; ₹30,000; ₹30,000; ₹40,000 and ₹60,000 respectively.

(II) *C* agrees to contribute 1/4 of the combined capital of *A* and *B* in the new firm.

(III) Plant is to be written down to ₹80,000 and Patents written up to ₹12,000. A provision of 2% on debtors is required. A liability of ₹5,000 included in Sundry Creditors is not likely to arise.

Give the Journal entries and Balance Sheet after the admission of *C*.

[**Ans.** Loss on Revaluation ₹14,000; Capital Accounts *A* ₹1,71,500; *B* ₹70,500 and *C* ₹60,500; *C*'s Current A/c (Dr.) ₹6,000; Cash Balance ₹78,500; B/S Total ₹3,67,500.]

Hints : C's share of goodwill has been debited to his Current A/c instead of Capital A/c.

Q. 117. Neha and Tara are partners in a firm sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as at 31st March, 2012, stood as follows :

Liabilities		₹	*Assets*		₹
Capital Accounts :			Plant & Machinery		12,000
Neha	8,000		Land and Building		14,000
Tara	10,000	18,000	Debtors	19,000	
General Reserve		12,000	*Less* : Provision for		
Workmen's Compensation Fund		5,000	Doubtful Debts	(4,000)	15,000
Creditors		15,000	Stock		6,000
			Cash		3,000
		50,000			50,000

They agreed to admit prachi into partnership for 1/5th share of profits on 1st April, 2012, on the following terms :

(*a*) All debtors to be considered as good and therefore the provision for doubtful debts to be written back.

(*b*) Value of land and building to be increased to ₹18,000.

(*c*) Value of plant and machinery to be reduced by ₹2,000.

(*d*) The liability against Workmen's Compensation Fund is determined at ₹2,000 which is to be paid later in the year.

(*e*) Prachi to bring in her share of Goodwill of ₹10,000 in cash.

(*f*) She will further bring in cash so as to make her capital equal to 20% of the total capital of the new firm : (Show your workings clearly).

You are required to prepare :

(*i*) Revaluation Account.

(*ii*) Partners' Capital Accounts.

(*iii*) Balance Sheet of the reconstituted firm. *(I.S.C. 2013)*

[**Ans.** Profit on Revaluation ₹6,000; Partner's Capital Accounts : Neha ₹26,600; Tara ₹22,400 and Prachi ₹12,250; Balance Sheet Total ₹78,250.]

Hint : Provision for Doubtful Debts will be shown on the Cr. side of Revaluation Account and Debtors will be shown in the Balance Sheet at ₹19,000.

Adjustment of Capitals of Old Partners

Q. 118. Balance Sheet as at 31st March, 2020 of Ramesh, Kumar and Pappu who were sharing profits and losses in the ratio of 2 : 3 : 5.

Liabilities	₹	*Assets*	₹
Capitals :		Cash	18,000
Ramesh	36,000	Bills Receivable	24,000
Kumar	44,000	Furniture	28,000
Pappu	52,000	Stock	44,000
Creditors	64,000	Debtors	42,000
Bills Payable	32,000	Investments	32,000

Profit & Loss A/c	14,000	Machinery	34,000
		Goodwill	20,000
	2,42,000		2,42,000

On 1st April, 2020 they admit Shilpa into partnership on the following terms :

1. Furniture, Investments and Machinery to be reduced by 15%.
2. The value of stock to be taken at ₹48,000.
3. Shilpa will bring in ₹26,000 as her share of goodwill.
4. Shilpa to bring ₹32,000 towards capital for 1/6th share and old partners to adjust their capitals accordingly.
5. Outstanding rent amounted to ₹1,800.
6. Prepaid salaries ₹800.
7. Adjustments of capitals to be made by cash.

Prepare Revaluation Account, Capital Accounts, Cash Account and the Balance Sheet of the new firm.

[**Ans.** Loss on Revaluation ₹11,100; Capital Accounts : Ramesh ₹32,000; Kumar ₹48,000; Pappu ₹80,000 and Shilpa ₹32,000; Cash balance ₹95,100; B/S Total ₹2,89,800; Ramesh withdraws ₹5,780; Kumar brings in ₹1,330 and Pappu brings in ₹23,550.]

Q. 119. *A* and *B* share profits in the ratio of 2 : 1. Their balance sheet as at 31st March, 2022 was as follows :

Liabilities		₹	*Assets*	₹
Provision for Doubtful Debts		800	Cash at Bank	6,000
Bank Overdraft		24,000	Sundry Debtors	20,000
Sundry Creditors		25,200	Stock	40,000
Capitals : *A*	60,000		Building	66,000
B	40,000	1,00,000	P & L Account	18,000
		1,50,000		1,50,000

C is admitted into partnership on 1st April, 2022 on the following terms :

(*i*) New profit sharing ratio will be 4 : 3 : 2 and *C* will pay ₹40,000 as his capital.

(*ii*) Goodwill of the firm is valued at ₹45,000 but *C* is unable to bring any amount for goodwill.

(*iii*) The provision for doubtful debts is to be raised to ₹2,000.

(*iv*) Stock be depreciated by ₹5,000.

(*v*) Provision be made for outstanding expenses amounting to ₹2,800.

(*vi*) Capitals of *A* and *B* be adjusted on the basis of new partners' capital and the actual cash to be paid off or brought in, as the case may be.

Prepare Journal entries, capital accounts, and the opening Balance Sheet of the new firm.

[**Ans.** Loss on Revaluation ₹9,000; Capital Accounts *A* ₹80,000; *B* ₹60,000 and *C* ₹40,000; Cash at bank ₹79,000; *A* brings in ₹28,000 and *B* brings in ₹29,000; B/S Total ₹2,10,000.]

Hints: 1. Provision for Doubtful Debts will be shown in liabilities at ₹2,000.

2. Bank Overdraft will be adjusted from Cash at Bank.

3. *C*'s share of goodwill will be debited to his Current Account instead of his Capital Account.

Q. 120. On 31-3-2022 the Balance Sheet of *W* and *R* who shared profits in 3 : 2 ratio was as follows :

Liabilities		₹	*Assets*		₹
Creditors		20,000	Cash		5,000
Profit and Loss Account		15,000	Sundry Debtors	20,000	
Capital Accounts :			*Less* : Provision	700	19,300
W	40,000		Stock		25,000
R	30,000	70,000	Plant and Machinery		35,000
			Patents		20,700
		1,05,000			1,05,000

On 1st April, 2022 *B* was admitted as a partner on the following conditions :

(*a*) *B* will get 4⁄15th share of profits.

(*b*) *B* had to bring ₹30,000 as his capital to which amount other Partners capitals shall have to be adjusted.

(*c*) He would pay cash for his share of goodwill which would be based on 2½ years purchase of average profits of past 4 years.

(*d*) The assets would be revalued as under :
Sundry debtors at book value *less* 5% provision for bad debts. Stock at ₹20,000, Plant and Machinery at ₹40,000.

(*e*) The profits of the firm for the years 2019, 2020 and 2021 were ₹20,000; ₹14,000 and ₹17,000 respectively.

Prepare Revaluation Account, Partner's Capital Accounts and the Balance Sheet of the new firm.

[**Ans.** Loss on Revaluation ₹300; New Ratio 33 : 22 : 20; Capital Accounts : *W* ₹49,500; *R* ₹33,000 and *B* ₹30,000; Cash Balance ₹32,800; B/S Total ₹1,32,500; *W* withdraws ₹5,920 and *R* withdraws ₹7,280.]

Hint : Average Profits $= \dfrac{20{,}000 + 14{,}000 + 17{,}000 + 15{,}000 \text{ (Given in Balance Sheet)}}{4}$

$= ₹16{,}500$

Value of Goodwill $= ₹16{,}500 \times 2\frac{1}{2} = ₹41{,}250$

B's Share in Goodwill $= ₹41{,}250 \times \dfrac{4}{15} = ₹11{,}000$

Q. 121. *A* and *B* are partners sharing profits in the ratio of 2 : 3. Their balance sheet as at 31st March, 2020 was as follows :

Liabilities		₹	Assets		₹
Bank Overdraft		32,000	Cash in Hand		3,000
Creditors		25,000	Cash at Bank		12,000
P & L Account		10,000	Debtors	40,000	
Capitals :			*Less* : Provision	5,000	35,000
A	1,00,000		Furniture		40,000
B	1,05,000	2,05,000	Building		80,000
			Machinery		1,00,000
			Investments		2,000
		2,72,000			2,72,000

On 1st April, 2020 they admitted *C* for 1/5 share in profits which he acquires wholly from *B*. The other terms of agreement were :

(*i*) Goodwill of the firm was to be valued at two years' purchase of the average of the last 3 years' profits. The profit for the last 3 years were ₹58,000; ₹66,000 and ₹56,000 respectively.

(*ii*) Provision for Doubtful debts was found in excess by ₹2,000.

(*iii*) Buildings were found undervalued by ₹20,000 and furniture overvalued by ₹5,000.

(*iv*) ₹5,000 for damages claimed by a customer had been disputed by the firm. It was agreed at ₹2,000 by a compromise between the customer and the firm.

(*v*) *C* was to bring in ₹60,000 as his capital and the necessary amount for his share of goodwill.

(*vi*) Capitals of *A* and *B* were to be adjusted in the new profit sharing ratio by opening necessary current accounts.

Prepare journal entries, capital accounts and the opening balance sheet.

[**Ans.** Profit on Revaluation ₹15,000; Capitals *A* ₹1,20,000; *B* ₹1,20,000 and *C* ₹60,000; Cash in Hand ₹3,000; Cash at Bank (after deducting bank overdraft) ₹64,000. B/S Total ₹3,51,000; New Ratio 2 : 2 : 1; *A*'s Current A/c ₹10,000 (Dr.); *B*'s Current A/c ₹24,000 (Cr.).]

Hint : No entry will be passed for ₹5,000. Only the following entry will be passed in respect of damages :

Revaluation A/c	Dr.	2,000	
To Damages Payable A/c			2,000

Q. 122. *A* and *B* are in partnership sharing profits and losses in the proportion of three-fourths and one-fourth respectively. Their Balance Sheet as at 31st March, 2022 was as follows :

Liabilities	₹	Assets	₹
Sundry Creditors	1,20,000	Cash	10,000
Bank Overdraft	1,50,000	Sundry Debtors	2,50,000
A's Capital	1,50,000	Stock	2,20,000
B's Capital	1,00,000	Plant and Machinery	40,000
	5,20,000		5,20,000

On 1st April, 2022 they admitted *C* into partnership on the following terms :

(*a*) *C* to purchase one-third of the goodwill for ₹20,000 and provide ₹1,00,000 as capital.

(*b*) Future profits and losses are to be shared by *A*, *B* and *C* equally.

(*c*) Plant and Machinery is to be reduced by 10% and ₹5,000 is to be provided for estimated bad debts. Stock is to be taken at a valuation of ₹2,49,400.

(*d*) By bringing in or withdrawing cash, capitals of *A* and *B* are to be made proportionate to that of *C* on their profit sharing basis.

Set out entries relating to the above arrangement in the firm's Journal, give the partners' Capital Accounts in tabular form and submit the opening Balance Sheet of the new firm.

[**Ans.** Profit on Revaluation ₹20,400; Capital Accounts ₹1,00,000 each; Total of Balance Sheet ₹5,70,000; Cash balance ₹39,600. Surplus Capital withdrawn by *A* and *B* ₹90,300 and ₹100 respectively.]

Hint : *A* sacrifices $\frac{5}{12}$; *B* gains $\frac{1}{12}$. *B* will also compensate *A* for acquiring $\frac{1}{12}$ share. Amount of compensation on the basis of premium paid by *C* will be ₹5,000.

Q. 123. *A* and *B* are partners in a firm sharing profits and losses in the ratio of 4 : 1, their Balance Sheet as at 31st March, 2022 is as follows :

Liabilities		₹	*Assets*	₹
Capital A/cs :			Furniture	20,000
A	25,000		Stock	40,000
B	65,000	90,000	Bills receivable	10,000
Reserve		20,000	Debtors	30,000
Creditors		25,000	Cash at Bank	40,000
Bills Payable		5,000		
		1,40,000		1,40,000

They agreed to take *C* as a partner with effect from 1st April, 2022 on the following terms :

(*a*) *A*, *B* and *C* will share profits and losses in the ratio of 5 : 3 : 2.

(*b*) *C* will bring ₹20,000 as premium for goodwill and ₹30,000 as capital.

(*c*) Half of the Reserve is to be withdrawn by the partners.

(*d*) The assets will be revalued as follows :

	₹
Furniture	30,000
Stock	39,500
Debtors	28,500

(*e*) *A* creditor for ₹12,000 has agreed to forgo his claim by ₹2,000.

(*f*) After making the above adjustments, the Capital Accounts of *A* and *B* should be adjusted on the basis of *C*'s capital by bringing cash or withdrawing cash, as the case may be.

Pass necessary Journal entries and prepare the Balance Sheet of the new firm.

[**Ans.** Profit on Revaluation ₹10,000; Capital Accounts *A* ₹75,000; *B* ₹45,000 and *C* ₹30,000; B/S Total ₹1,78,000. Cash at Bank ₹70,000.]

Hints : (*i*) Reserve of ₹20,000 will be credited to the Capital Accounts of *A* and *B* in the ratio of 4 : 1. Thereafter, *A* and *B* will withdraw cash through their Capital Accounts ₹8,000 and ₹2,000 respectively.

(*ii*) Creditors will appear in the Balance Sheet at ₹23,000.

(*iii*) *A* sacrifices $\frac{3}{10}$ whereas *B* gains $\frac{1}{10}$. Hence, *B* will compensate *A* for goodwill. The amount of compensation (based on premium for goodwill brought in by *C*) will be ₹10,000.

(*iv*) Capitals of *A* and *B* after all adjustments are arrived at ₹71,000 and ₹59,000 respectively whereas their adjusted capitals based on *C*'s capital should be ₹75,000 and ₹45,000. Hence, *A* brings in ₹4,000 and *B* withdraws ₹14,000.

Q. 124. Quick and Slow are partners in a firm sharing Profit and Losses in the ratio of 3 : 2. On 1st April, 2020 Smooth comes in for one-third share paying ₹5,000 premium and proportionate capital. Capitals of Quick and Slow are also to be adjusted in profit-sharing ratio. The Balance Sheet of Quick and Slow before Smooth comes in stands as below :

Liabilities		₹	*Assets*	₹
Capital Account :			Machinery	32,000
Quick	29,000		Furniture	2,000
Slow	39,000	68,000	Stock	15,000
Reserve		10,000	Debtors	40,000
Creditors		12,000	Cash	6,000
Outstanding Expenses		5,000		
		95,000		95,000

Machinery is valued at ₹30,000, stock at ₹23,000. Debtors are considered worth ₹38,000. One trade creditor for ₹1,000 is due for many years and he is not traceable. On the other hand one contingent liability for expenses ₹500 had matured and it is not recorded in the books. Reserve Account is not to be shown in Accounts.

Prepare Profit and Loss Adjustment Account and Balance Sheet after admission of Smooth.

[**Ans.** Profit on Revaluation ₹4,500; Capital Accounts : Quick ₹52,500; Slow ₹35,000 and Smooth ₹43,750; B/S Total ₹1,47,750. New Profit Sharing Ratio 6 : 4 : 5.]

Hint : Total capital of Quick and Slow after all adjustments = 40,700 + 46,800 = 87,500. Since their combined share in profits is $\frac{10}{15}$, total capital of the firm must be = 87,500 × $\frac{15}{10}$ = ₹1,31,250.

∴ Quick's adjusted Capital $= 1,31,250 \times \frac{6}{15}$ = 52,500

Slow's adjusted Capital $= 1,31,250 \times \frac{4}{15}$ = 35,000

Amount brought in by Quick = 52,500 – 40,700 = 11,800

Amount withdrawn by Slow = 46,800 – 35,000 = 11,800

Q. 125. Abha and Bimal are partners in a firm sharing profits and losses in the ratio of 3 : 2. On 31st March, 2015 they admitted Chintu into partnership for 1/5th share in the profits of the firm. On that date their Balance sheet stood as under :

BALANCE SHEET *as at 31st March, 2015*

Liabilities			*Amount*	*Assets*	*Amount*
			₹		₹
Capitals :	Abha	1,20,000		Plant and Machinery	1,30,000
	Bimal	1,00,000	2,20,000	Furniture	25,000
General Reserve			20,000	Investments	1,00,000
Sundry Creditors			1,00,000	Sundry Debtors	50,000
				Bank	35,000
			3,40,000		3,40,000

Chintu was admitted on the following terms :

(*i*) He will bring ₹80,000 as capital and ₹30,000 for his share of goodwill premium.

(*ii*) Partners will share future profits in the ratio of 5 : 3 : 2.

(*iii*) Profit on revaluation of assets and reassessment of liabilities was ₹7,000.

(*iv*) After making adjustments, the Capital Accounts of the partners will be in proportion to Chintu's capital. Balance to be paid off or brought in by the old partners by cheque as the case may be.

Prepare the Capital Accounts of the partners and Bank Account.

(C.B.S.E. 2016 Comptt., All India)

[**Ans.** Final Capitals : Abha ₹2,00,000, Bimal ₹1,20,000 and Chintu ₹80,000. Abha brings in ₹48,800 and Bimal withdraws ₹5,800. Bank balance ₹1,88,000]

Q. 126. John, Bull and Wool were in partnership, sharing profits and losses in the ratio of 2 : 2 : 1. Their Balance Sheet as at 31st March 2020, is given below :

Liabilities		₹	*Assets*	₹
Sundry Creditors		25,700	Land & Buildings	50,000
Outstanding Liabilities		3,000	Furniture	13,000
General Reserve		13,000	Stock of Goods	23,500
Capital Accounts :			Sundry Debtors	11,000
John	24,000		Cash	2,200
Bull	24,000			
Wool	10,000	58,000		
		99,700		99,700

The partners have agreed to take Tuna as a partner with effect from 1st April 2020, on the following terms :

(*a*) Tuna shall bring ₹10,000 towards his capital.

(*b*) The value of goodwill shall be fixed at ₹21,500.

(*c*) General Reserve is not to be distributed and the effect of admission is to be recorded by passing an adjustment entry. However, Tuna's capital is not to be affected.

(*d*) The value of the stock should be increased by ₹5,000. The furniture should be depreciated by 10%. The value of Land & Buildings should be enhanced by 20%.

(*e*) Provision for Doubtful Debts should be made at 10% of the debtors.

(*f*) The outstanding liabilities include ₹1,000 due to Mr. Grip, which has been paid by John privately. Necessary entry to reimburse Mr. John, as per his request, before admitting the new partner, has to be passed.

(*g*) The new profit-sharing ratio will be 5 : 5 : 3 : 2.

Prepare a Revaluation Account and the Capital Accounts of all the four partners. Also prepare a Balance Sheet of the new firm.

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Furniture A/c		1,300	By Stock A/c	5,000
To Provision for Doubtful Debts		1,100	By Land and Buildings A/c	10,000
To Profit transferred to :				
John's Capital A/c	5,040			
Bull's Capital A/c	5,040			
Wool's Capital A/c	2,520	12,600		
		15,000		15,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*John*	*Bull*	*Wool*	*Tuna*	*Particulars*	*John*	*Bull*	*Wool*	*Tuna*
	₹	₹	₹	₹		₹	₹	₹	₹
To Bal. c/d	32,340	31,340	12,520	10,000	By Bal. b/d	24,000	24,000	10,000	
					By Cash A/c				10,000
					By Tuna's Current A/c[1] (In sacrificing Ratio i.e. 1:1)	2,300	2,300	—	
					By Outstanding Liabilities A/c	1,000			
					By Revaluation (Profit)	5,040	5,040	2,520	
	32,340	31,340	12,520	10,000		32,340	31,340	12,520	10,000

BALANCE SHEET *as at 1st April 2020*

Liabilities		₹	*Assets*		₹
Sundry Creditors		25,700	Land & Buildings		60,000
Outstanding Liabilities		2,000	Furniture		11,700
General Reserve		13,000	Stock of Goods		28,500
Capital Accounts :			Sundry Debtors	11,000	
John	32,340		*Less :* Provision for		
Bull	31,340		Doubtful Debts	1,100	9,900

Wool	12,520		Cash	12,200
Tuna	10,000	86,200	Tuna's Current A/c	4,600
		1,26,900		1,26,900

Note :

	₹
(1) Adjustment to be made for :	
Goodwill	21,500
General Reserve	13,000
	34,500

Tuna's Current Account will be debited by ₹ $\frac{2}{15}$ of 34,500 and John and Bull Capital A/cs will be credited in sacrificing ratio of 1 : 1.

Q. 127. *A* and *B* are partners in the ratio of 3 : 2. Their Balance Sheet as at 31st March, 2022 appeared as follows :

Liabilities		₹	*Assets*	₹
Creditors		30,000	Plant	3,00,000
Workmen's Compensation			Stock	2,00,000
Reserve		15,000	Debtors	1,00,000
Capitals :			Bank	45,000
A	4,00,000			
B	2,00,000	6,00,000		
		6,45,000		6,45,000

The partners decide to admit *C* with effect from 1st April, 2022, on the following terms :

(*i*) *C* is to bring ₹1,00,000 as capital and ₹20,000 as his share of goodwill.

(*ii*) *C* can bring only ₹5,000 as goodwill in cash.

(*iii*) Plant is depreciated by 10% and stock by ₹10,000.

(*iv*) The liability on Workmen's Compensation Reserve is determined at ₹6,000. However, the book value of Workmen's Compensation Reserve appearing in the Balance Sheet is not to be altered. Adjustment is to be made through *C*'s Current A/c.

(*v*) Creditors include an amount of ₹8,000 received as commission.

(*vi*) A contingent liability of ₹5,000 not included in the above balance sheet had to be cleared.

(*vii*) The new profit-sharing ratio of *A*, *B* and *C* is 4 : 3 : 2.

Pass entries and prepare Capital Accounts and Balance Sheet of the new firm.

SOLUTION :

A, B and C
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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
April 1	C's Current A/c (9,000 × $\frac{2}{9}$)	Dr.		2,000	
	To A's Capital A/c				1,400
	To B's Capital A/c				600
	(Excess of Workmen's Compensation adjusted in sacrificing ratio of 7 : 3)				
	Bank A/c	Dr.		1,05,000	
	To C's Capital A/c				1,00,000
	To Premium A/c				5,000
	(Amount of capital and premium for goodwill brought in by C)				
	Premium A/c	Dr.		5,000	
	To A's Capital A/c				3,500
	To B's Capital A/c				1,500
	(Premium for goodwill credited to A and B in sacrificing ratio of 7 : 3)				
	C's Current A/c	Dr.		15,000	
	To A's Capital A/c				10,500
	To B's Capital A/c				4,500
	(Goodwill credited to old partners in their sacrificing ratio of 7 : 3)				
	Revaluation A/c	Dr.		45,000	
	To Plant A/c				30,000
	To Stock A/c				10,000
	To Bank A/c (Payment of Contingent Liability)				5,000
	(Decrease in the value of assets)				
	Creditors A/c	Dr.		8,000	
	To Revaluation A/c				8,000
	(Decrease in Creditors)				
	A's Capital A/c	Dr.		22,200	
	B's Capital A/c	Dr.		14,800	
	To Revaluation A/c				37,000
	(Transfer of loss on revaluation)				

Dr. **CAPITAL ACCOUNTS** Cr.

Particulars	A	B	C	Particulars	A	B	C
	₹	₹	₹		₹	₹	₹
To Revaluation	22,200	14,800		By Bal. b/d	4,00,000	2,00,000	
To Bal. c/d	[illegible]	[illegible]	1,00,000	By C's Current A/c	1,400	600	
				By Bank			1,00,000
				By Premium	3,500	1,500	

				By C's Current A/c (Goodwill)	10,500	4,500	
	4,15,400	2,06,600	1,00,000		4,15,400	2,06,600	1,00,000

BALANCE SHEET *as at 1st April, 2022*

Liabilities		₹	*Assets*	₹
Creditors		22,000	Plant	2,70,000
Workmen's Compensation			Stock	1,90,000
Reserve		15,000	Debtors	1,00,000
Capitals :			Bank	1,45,000
A	3,93,200		C's Current A/c	17,000
B	1,91,800			
C	1,00,000	6,85,000		
		7,22,000		7,22,000

Q. 128. Juliet and Rabani are partners in a firm, sharing profits and losses in the ratio of 3 : 1. On 31st March, 2016, their Balance Sheet was as under :

BALANCE SHEET OF JULIET AND RABANI

As at 31st March, 2016

Liabilities		₹	*Assets*		₹
Sundry Creditors		70,000	Plant and Machinery		1,76,000
General Reserve		30,000	Inventory		26,000
Provident Fund		40,000	Sundry Debtors	57,000	
Capital A/cs			*Less :* Provision for Doubtful Debts	3,000	54,000
Juliet	1,10,000		Cash at Bank		68,000
Rabani	90,000	2,00,000	Profit & Loss A/c		16,000
		3,40,000			3,40,000

Mike was taken as a partner for $\frac{1}{4}$th share, with effect from 1st April, 2016, subject to the following adjustments :

(*a*) Plant and Machinery was found to be overvalued by ₹16,000. It was to be shown in the books at the correct value.

(*b*) Provision for Doubtful Debts was to be reduced by ₹2,000.

(*c*) Creditors included an amount of ₹2,000 received as commission from Malini. The necessary adjustment was required to be made.

(*d*) Goodwill of the firm was valued at ₹60,000. Mike was to being in cash, his share of goodwill along with his capital of ₹1,00,000.

(*e*) Capital Accounts of Juliet and Rabani were to be readjusted in the new profit sharing arrangement on the basis of Mike's capital, any surplus to be adjusted through current account and any deficiency through cash.

You are required to prepare :

(i) Revaluation Account,

(ii) Partner's Capital Accounts, and

(iii) Balance Sheet of the reconstituted firm.

(I.S.C. 2017)

[**Ans.** Loss on Revaluation ₹12,000; Capital Accounts : Juliet ₹2,25,000 and Rabani ₹75,000; Juliet brings in ₹1,02,250; Rabani's Current Account (Cr.) ₹19,250; Cash at Bank ₹2,85,250; B/S total ₹5,27,250.]

Q. 129. Dhruv and Ansh are partners in a firm sharing profits and losses : Dhruv 75% and Ansh 25% respectively.

Their Balance Sheet as at 31st March, 2016 is given below :

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Sundry Creditors		39,000	Cash		10,000
Workmen Compensation Reserve		5,000	Sundry Debtors	18,500	
Profit & Loss Account		10,000	*Less :* Provision for Doubtful Debts	(1,500)	17,000
Capital Accounts :					
Dhruv	30,000		Stock		37,000
Ansh	20,000	50,000	Furniture		5,000
			Land & Buildings		25,000
			Goodwill		10,000
		1,04,000			1,04,000

On 1st April, 2016, Kavi is admitted as a new partner on the following terms :

(i) The value of stock is to be increased to ₹42,000.

(ii) Land and Building is to be reduced by 20%.

(iii) Bad Debts amounting to ₹1,800 are to be written off.

(iv) Creditors include an amount of ₹5,000 received as commission from Amar. The necessary adjustment is required to be made.

(v) The liability of Workmen Compensation Reserve is determined at ₹3,000.

(vi) Kavi is to pay ₹15,000 to the existing partners as premium for Goodwill for 20% of the future profits of the firm. He is also to bring in capital equal to $\frac{1}{4}$th of the combined capitals of Dhruv and Ansh.

You are required to :

(i) Pass journal entries on the date of Kavi's admission.

(ii) Prepare the opening Balance Sheet of the new firm on the completion of the transactions.

(I.S.C. Specimen Question Paper, 2017)

[**Ans.** Profit on Revaluation ₹4,700; Capital A/cs : Dhruv ₹46,275; Ansh ₹25,425 and Kavi ₹17,925; B/S Total ₹1,26,625.]

Q. 130. Sanjana and Alok were partners in a firm sharing profits and losses in the ratio 3 : 2. On 31st March, 2018 their Balance Sheet was as follows :

BALANCE SHEET OF SANJANA AND ALOK
as at 31.3.2018

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Creditors		60,000	Cash at Bank		1,66,000
Workmen's Compensation Reserve		60,000	Debtors	1,46,000	
			Less : Provision for Doubtful debts	2,000	1,44,000
Capitals :			Stock		1,50,000
Sanjana	5,00,000		Investments		2,60,000
Alok	4,00,000	9,00,000	Furniture		3,00,000
		10,20,000			10,20,000

On 1st April, 2018, they admitted Nidhi as a new partner for 1/4th share in the profits on the following terms :

(*a*) Goodwill of the firm was valued at ₹4,00,000 and Nidhi brought the necessary amount in cash for her share of goodwill premium, half of which was withdrawn by the old partners.

(*b*) Stock was to be increased by 20% and furniture was to be reduced to 90%.

(*c*) Investments were to be valued at ₹3,00,000. Alok took over investments at this value.

(*d*) Nidhi brought ₹3,00,000 as her capital and the capitals of Sanjana and Alok were adjusted in the new profit sharing ratio.

Prepare Revaluation Account, Partners Capital Accounts and the Balance Sheet of the reconstituted firm on Nidhi's admission. *(C.B.S.E. 2019, M.P.)*

[**Ans.** Profit on Revaluation ₹40,000; Capital A/cs : Sanjana ₹5,40,000; Alok ₹3,60,000 and Nidhi ₹3,00,000; Sanjana withdraws ₹50,000 and Alok brings in ₹2,00,000; Balance Sheet Total ₹12,60,000.]

Q. 131. Smita and Punita are partners in a firm sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as at 31st March, 2019, is as follows :

BALANCE SHEET OF SMITA AND PUNITA
as at 31st March, 2019

Liabilities		₹	*Assets*		₹
Sundry Creditors		14,000	Cash in Hand		30,000
Bank Loan		6,000	Sundry Debtors.	22,000	
General Reserve		10,000	*Less* : Provision for Doubtful Debts	(2,000)	20,000
Capital Accounts :			Furniture		10,000
Smita	30,000				
Punita	40,000	70,000	Stock		40,000
		1,00,000			1,00,000

On 1st April, 2019, Mita is admitted as a new partner on the following terms :

(*a*) The new profit sharing ratio of Smita, Punita and Mita to be 5 : 3 : 2.

(*b*) Provision for doubtful debts to be raised to 10% of the debtors.

(*c*) Punita to take over the firm's investments (not recorded in the books) at ₹3,000.

(*d*) Goodwill of the firm to be valued at ₹50,000. Mita to bring in cash for her share of goodwill.

(*e*) 50% of the goodwill to be withdrawn by the old partners.

(*f*) Mita to pay off the Bank Loan on behalf of the firm. The amount due to her by the firm, to be considered as part of her capital contribution.

(*g*) Mita to bring in the balance of her capital in cash, so as to make her capital equal to 1/5th of the total capital of the firm.

You are required to :

(*i*) Pass journal entries at the time of Mita's admission.

(*ii*) Prepare the Balance Sheet of the reconstituted firm. *(I.S.C. 2020)*

[**Ans.** Gain on Revaluation ₹2,800; Smita's Capital ₹40,180; Punita's Capital ₹44,620; Mita's Capital ₹21,200 (Out of which ₹6,000 transferrfed from Bank Loan A/c and ₹15,200 brought in Cash); Balance Sheet Total ₹1,20,000.]

MULTIPLE CHOICE QUESTIONS

Choose the Best Alternate :

1. A new partner may be admitted into a partnership :
   (A) With the consent of any one partner
   (B) With the consent of majority of partners
   (C) With the consent of all old partners
   (D) With the consent of 2/3rd of old partners

2. On the admission of a new partner :
   (A) Old firm is dissolved
   (B) Old partnership is dissolved
   (C) Both old partnership and firm are dissolved
   (D) Neither partnership nor firm is dissolved

Calculation of New Profit Sharing Ratios :

3. *A* and *B* are partners sharing profit in the ratio of 3 : 2. They admit *C* as a partner by giving him 1/3 share in future profits. The new ratio will be :
   (A) 12 : 8 : 5 (B) 8: 12 : 5
   (C) 5 : 5 : 12 (D) None of the Above

4. *X* and *Y* are partners sharing profit in the ratio of 3 : 2. *Z* was admitted with 1/4 share in profits which he acquires equally from *X* and *Y*. The new ratio will be:
   (A) 9 : 6 : 5 (B) 19 : 11 : 10
   (C) 3 : 3 : 2 (D) 3 : 2 : 4

5. A and B share profits in the ratio of 2 : 1. C is admitted with 1/4 share in profits. C acquires 3/4 of his share from A and 1/4 of his share from B. The new ratio will be:
   (A) 2 : 1 : 1
   (B) 23 : 13 : 12
   (C) 3 : 1 : 1
   (D) 13 : 23 : 12

6. B and N are partners in a firm sharing profits in the ratio of 3 : 2. They admit S as a partner for 1/4th share in the profits. S acquires his share from B and N in the ratio of 2 : 1. The new profit-sharing ratio will be :
   (A) 2 : 1 : 4
   (B) 19 : 26 : 15
   (C) 3 : 2 : 4
   (D) 26 : 19 : 15

7. A and B are partners sharing profits and losses in the ratio of 7 : 5. They agree to admit C, their manager, into partnership who is to get 1/6th share in the profits. He acquires this share as 1/24th from A and 1/8th from B. The new profit sharing ratio will be :
   (A) 13 : 7 : 4
   (B) 7 : 13 : 4
   (C) 7 : 5 : 6
   (D) 5 : 7 : 6

8. A and B share profits in the ratio of 3 : 2. They agreed to admit C on the condition that A will sacrifice $\frac{3}{25}$th of his share of profit in favour of C and B will sacrifice $\frac{1}{25}$th of his profits in favour of C. The new profit sharing ratio will be :
   (A) 12 : 9 : 4
   (B) 3 : 2 : 4
   (C) 66 : 48 : 11
   (D) 48 : 66 : 11

9. A and B are partners in a firm sharing profits and losses in the ratio of 3 : 2. A new partner C is admitted. A surrenders 1/15th share of his profit in favour of C and B surrenders 2/15th of his share in favour of C. The new ratio will be :
   (A) 8 : 4 : 3
   (B) 42 : 26 : 7
   (C) 4 : 8 : 3
   (D) 26 : 42 : 7

10. A and B are partners sharing profit or loss in the ratio of 4 : 1. A surrenders 1/4 of his share and B surrenders 1/2 of his share in favour of C, a new partner. What will be the C's share?
   (A) $\frac{3}{4}$
   (B) $\frac{1}{5}$
   (C) $\frac{1}{10}$
   (D) $\frac{3}{10}$

11. A and B are partners in a business sharing profits and losses in the ratio of 7 : 3 respectively. They admit C as a new partner. A sacrificed 1/7th share of his profit and B sacrificed 1/3rd of his share in favour of C. The new profit sharing ratio of A, B and C will be :
   (A) 3 : 1 : 1
   (B) 2 : 1 : 1
   (C) 2 : 2 : 1
   (D) None of the above

12. A and B are partners sharing profit or loss in the ratio of 3 : 2. C is admitted into partnership as a new partner. A sacrifices 1/3 of his share of B sacrifices 1/4 of his share in favour of C. What will be the C's share in the firm?

(A) $\frac{1}{5}$ (B) $\frac{2}{10}$
(C) $\frac{3}{10}$ (D) None of the above

13. Niyati and Aisha were partners in a firm sharing profit and losses in the ratio of 4 : 3. They admitted Bina as a new partner. Niyati sacrificed $\frac{1}{4}$th from her share and Aisha sacrificed $\frac{1}{7}$th from her share in favour of Bina. Bina's share in the profits of the firm will be :

(A) $\frac{2}{7}$ (B) $\frac{10}{49}$
(C) $\frac{11}{28}$ (D) $\frac{7}{16}$

(C.B.S.E. 2020, Rajasthan)

14. A and B are partners in a firm sharing profits and losses in the ratio of 2 : 3. C is admitted for 1/5 share in the profits of the firm. If C gets it wholly from A, the new profit sharing ratio after C's admission will be :

(A) 1 : 3 : 3 (B) 3 : 1 : 1
(C) 2 : 2 : 1 (D) 1 : 3 : 1

(C.B.S.E. 2020, Kerala)

15. A and B are partners sharing profits in the ratio of 4 : 3. They admitted C as a new partner who gets 1/5th share of profit, entirely from A. The new profit sharing ratio will be :

(A) 20 : 8 : 7 (B) 13 : 15 : 15
(C) 13 : 15 : 7 (D) 15 : 13 : 5

16. A, B, C, D are in partnership sharing profits and losses in the ratio of 9 : 6 : 5 : 5. E joins the partnership for 20% share. A, B, C and D would in future share profits among themselves as 3/10 : 4/10 : 2/10 : 1/10. The new profit sharing ratio will be:

(A) 3 : 4 : 2 : 1 : 5 (B) 9 : 6 : 5 : 5 : 5
(C) 6 : 8 : 4 : 2 : 5 (D) 8 : 6 : 4 : 2 : 5

17. A and B are in partnership sharing profits and losses as 3 : 2. C is admitted for 1/4th share. Afterwards D enters for 20 paisa in the rupee. The new profit sharing ratio after D's admission will be :

(A) 9 : 6 : 5 : 5 (B) 6 : 9 : 5 : 5
(C) 3 : 2 : 4 : 5 (D) 3 : 2 : 5 : 5

Calculation of Sacrificing Ratio :

18. The formula for calculating the sacrificing ratio is :

(A) New share – Old share (B) Old share – New share
(C) Gaining Ratio – Old Ratio (D) Old Ratio – Gaining Ratio

19. X and Y are partners sharing profits in the ratio of 3 : 2. Z is admitted as a partner. Calculate sacrificing ratio if new profit sharing ratio is 9 : 7 : 4.
(A) 3 : 1
(B) 3 : 2
(C) 1 : 3
(D) 9 : 7

20. Veena and Soma are partners in a firm. They admit Sara on 1st April, 2020, for ¼ share in the profits of the firm. Sara acquired her share as $\frac{1}{12}$ from Veena and the remaining from Soma.
The sacrificing ratio of the old partners will be:
(A) 11 : 12
(B) 1 : 1
(C) 1 : 2
(D) 1 : 11
(I.S.C. Sample Paper, 2021)

21. Bishan and Sudha were partners in a firm sharing profits and losses in the ratio of 5 : 3. Alena was admitted as a new partner. It was decided that the new profit sharing ratio of Bishan, Sudha and Alena will be 10 : 6 : 5. The sacrificing ratio of Bishan and Sudha will be :
(A) 5 : 3
(B) 25 : 78
(C) 6 : 5
(D) 2 : 1 *(C.B.S.E. 2020, Kerala)*

22. A and B are partners sharing profits in the ratio of 5 : 3. A surrenders $\frac{1}{4}$th of his share and B surrenders $\frac{1}{5}$ of his share in favour of C, a new partner. What is the sacrificing ratio?
(A) 4 : 5
(B) 5 : 4
(C) 12 : 25
(D) 25 : 12

23. A and B are partners sharing profits in the ratio of 11 : 4. C was admitted. A surrendered $\frac{1}{11}$th of his share and B $\frac{1}{4}$ of his share in favour of C. The sacrificing ratio will be :
(A) 11 : 4
(B) 1 : 1
(C) 4 : 11
(D) 7 : 4

24. P and Q are partners sharing profits in the ratio of 9 : 7. R is admitted as a partner with $\frac{9}{20}$th share in the profits, which he takes $\frac{1}{5}$th from P and $\frac{1}{4}$th from Q. Sacrificing ratio will be :
(A) 5 : 4
(B) 9 : 7
(C) 7 : 9
(D) 4 : 5

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25. A, B and C are partners sharing in the ratio of 5 : 4 : 3. They admit D for $\frac{1}{7}$th share. It is agreed that B would retain his original share. Sacrificing ratio will be :
(A) A, B and C — 5 : 4 : 3
(B) A and C — 4 : 3
(C) A and C — 5 : 4
(D) A and C — 5 : 3

26. A and B are partners sharing profits and losses in the ratio of 5 : 4. C is admitted for $\frac{1}{5}$th share. A and B decide to share equally in future. Sacrificing ratio will be :

(A) 5 : 4
(B) 2 : 7
(C) 7 : 2
(D) 1 : 1

27. A and B are partners. They admit C for $\frac{1}{3}$rd share. In future the ratio between A and B would be 2 : 1. Sacrificing ratio will be :

(A) 2 : 1
(B) 1 : 1
(C) 5 : 1
(D) 1 : 5

Treatment of Goodwill :

28. Aditya and Shiv were partners in a firm with capitals of ₹3,00,000 and ₹2,00,000, respectively. Naina was admitted as a new partner for $\frac{1}{4}$th share in the profits of the firm. Naina brought ₹1,20,000 for her share of goodwill premium and ₹2,40,000 for her capital. The amount of goodwill premium credited to Aditya will be :

(A) ₹40,000
(B) ₹30,000
(C) ₹72,000
(D) ₹60,000

(C.B.S.E. 2020, Chennai, Kolkata)

29. A and B are partners sharing profits and losses as 2 : 1. C is admitted and profit sharing ratio becomes 4 : 3 : 2. Goodwill is valued at ₹94,500. C brings required goodwill in cash. Goodwill amount will be Credited to :

(A) A ₹14,000 and B ₹7,000
(B) A ₹12,000 and B ₹9,000
(C) A ₹21,000
(D) A ₹94,500

30. Kalki and Kumud were partners sharing profits and losses in the ratio of 5 : 3. On 1st April, 2021 they admitted Kaushtubh as a new partner and new ratio was decided as 3 :2 :1.

Goodwill of the firm was valued as ₹3,60,000. Kaushtubh couldn't bring any amount for goodwill. Amount of goodwill share to be credited to Kalki and Kumud Account's will be:

(A) ₹37,500 and ₹22,500 respectively
(B) ₹30,000 and ₹30,000 respectively
(C) ₹36,000 and ₹24,000 respectively
(D) ₹45,000 and ₹15,000 respectively

(C.B.S.E. Sample Paper, 2021)

31. Asha and Nisha are partner's sharing profits in the ratio of 2 :1. Kashish was admitted for 1/4 share out of which 1/8 was gifted by Asha. The remaining was contributed by Nisha. Goodwill of the firm is valued at ₹40,000. How much amount for goodwill will be credited to Nisha's Capital account?

(A) ₹ 2,500
(B) ₹ 5,000
(C) ₹20,000
(D) ₹40,000

(C.B.S.E. Sample Paper, 2021)

32. *X* and *Y* are partners sharing profits and losses in the ratio of 3 : 2. They admit *Z* into partnership with $\frac{1}{5}$th share in profits which he acquires equally from *X* and *Y*. *Z* brings in ₹40,000 as goodwill in cash. Goodwill amount will be credited to :
(A) *X* ₹20,000; *Y* ₹20,000
(B) *X* ₹25,000; *Y* ₹15,000
(C) *X* ₹24,000; *Y* ₹16,000
(D) *X* ₹ 4,000; *Y* ₹ 4,000

33. *A* and *B* are partners sharing profits and losses in the ratio of 3 : 2. *C* is admitted into partnership for $\frac{1}{5}$th share in profit. He pays ₹1,00,000 as goodwill. The ratio of the partners *A*, *B* and *C* in the new firm would be 3 : 1 : 1. Goodwill will be credited to:
(A) Only *A* ₹1,00,000
(B) Only *B* ₹1,00,000
(C) *A* ₹60,000; *B* ₹40,000
(D) *A* ₹75,000; *B* ₹25,000

34. *A* and *B* are partners in a firm sharing profits in the ratio of 2 : 1. *C* is admitted as a partner. *A* and *B* surrender $\frac{1}{2}$ of their respective share in favour of *C*. *C* is to bring his share of premium for goodwill in cash. The goodwill of the firm is estimated at ₹ 60,000. Credit will be given to :
(A) *A* ₹15,000; *B* ₹15,000
(B) *A* ₹40,000; *B* ₹20,000
(C) *A* ₹30,000; *B* ₹30,000
(D) *A* ₹20,000; *B* ₹10,000

HOTS

35. *P* and *S* are partners sharing profits in the ratio of 3 : 2. *R* is admitted with $\frac{1}{5}$th share and he brings in ₹84,000 as his share of goodwill which is Credited to the Capital Accounts of *P* and *S* respectively with ₹63,000 and ₹21,000. New profit sharing ratio will be :
(A) 3 : 1 : 5
(B) 9 : 7 : 4
(C) 3 : 2 : 5
(D) 7 : 9 : 4

36. Partners *A*, *B* and *C* share the profits of a business in the ratio of 3 : 2 : 1 respectively. They admit *D* who brings in ₹60,000 for his share of goodwill. *A*, *B*, *C* and *D* decide to share the profits respectively in the ratio of 5 : 3 : 2 : 2. Credit will be given to :
(A) *A* ₹ 6,000; *B* ₹6,000
(B) *A* ₹30,000; *B* ₹18,000; *C* ₹12,000
(C) *A* ₹30,000; *B* ₹20,000; *C* ₹10,000
(D) *A* ₹30,000; *B* ₹30,000

37. Anita and Babita were partners sharing profits and losses in the ratio of 3 : 1. Savita was admitted for $\frac{1}{5}$th share in the profits. Savita was unable to bring her share of goodwill premium in cash. The journal entry recorded for goodwill premium is given below :

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Savita's Current A/c	Dr.		24,000	
	To Anita's Capital A/c				8,000
	To Babita's Capital A/c				16,000
	(Adjustment of goodwill premium on Savita's Admission)				

The new profit sharing ratio of Anita, Babita and Savita, will be

(A) 41 : 7 : 12 (B) 13 : 12 : 10

(C) 3 : 1 : 1 (D) 5 : 3 : 2

(C.B.S.E. 2020; Punjab)

38. *A* and *B* are partners sharing profits and losses as 2 : 1. *C* and *D* are admitted and profit sharing ratio becomes 3 : 2 : 4 : 1. Goodwill is valued at ₹90,000. *C* and *D* bring required goodwill in Cash. Credit will be given to :

(A) *A* ₹30,000; *B* ₹15,000 (B) *A* ₹66,000; *B* ₹24,000

(C) *A* ₹33,000; *B* ₹12,000 (D) *A* ₹27,000; *B* ₹18,000

39. *A* and *B* are partners sharing profits and losses in 3 : 2. They admit *C* into partnership for $\frac{3}{10}$th share in the profits. *A* surrenders $\frac{1}{3}$rd of his share and *B* surrenders $\frac{1}{4}$th of his share in favour of *C*. Goodwill of the firm is valued at ₹3,00,000 but *C* is unable to bring his share of goodwill in cash. Credit will be given to :

(A) *A* ₹ 54,000; *B* ₹ 36,000 (B) *A* ₹ 60,000; *B* ₹ 30,000

(C) *A* ₹2,00,000; *B* ₹1,00,000 (D) *A* ₹1,80,000; *B* ₹1,20,000

40. *A* and *B* are partners sharing profits in the ratio of 7 : 5. *C* is admitted into the partnership for $\frac{1}{6}$th share which he acquires $\frac{1}{24}$th from *A* and $\frac{1}{8}$th from *B*. *C* does not pay anything for his share of goodwill. On *C*'s admission firm's goodwill was valued at ₹1,80,000. Credit will be given to :

(A) *A* ₹ 22,500; *B* ₹ 7,500 (B) *A* ₹ 7,500; *B* ₹ 22,500

(C) *A* ₹ 45,000; *B* ₹1,35,000 (D) *A* ₹1,35,000; *B* ₹ 45,000

41. *X* and *Y* are partners in a firm sharing profits in the ratio of 5 : 3. They admitted *Z* as a new partner. The new profit sharing ratio will be 4 : 3 : 2. The firm's goodwill on *Z*'s admission was valued at ₹1,26,000. But *Z* could not bring any amount of goodwill in Cash. Credit will be given to :

(A) *X* ₹ 17,500; *Y* ₹10,500 (B) *X* ₹ 16,000; *Y* ₹12,000

(C) *X* ₹ 22,750; *Y* ₹ 5,250 (D) *X* ₹1,02,375; *Y* ₹23,625

42. *A* and *B* are partners sharing profits in the ratio of 3 : 2. They admit *C* into the partnership with $\frac{1}{4}$th share in future profits. The new profit sharing ratio is 5 : 4 : 3. The firm's goodwill on *C*'s admission was valued at ₹1,44,000. But *C* could not bring any amount for goodwill in Cash. Credit will be given to :

(A) *A* ₹ 80,000; *B* ₹64,000 (B) *A* ₹ 20,000; *B* ₹16,000

(C) *A* ₹1,05,600; *B* ₹38,400 (D) *A* ₹ 26,400; *B* ₹ 9,600

43. P, Q and R share profits in the ratio of 5 : 3 : 2. S is entitled for $\frac{1}{5}$th share in profits which he acquires equally from P, Q and R. Goodwill of the firm is to be valued at three year's purchase of last four year's profits which are ₹50,000; ₹60,000; (–) ₹30,000 and ₹40,000. S cannot bring his share of goodwill in cash. Credit will be given to :

(A) P ₹30,000; Q ₹30,000; R ₹30,000
(B) P ₹ 6,000; Q ₹ 6,000; R ₹ 6,000
(C) P ₹45,000; Q ₹27,000; R ₹18,000
(D) P ₹ 9,000; Q ₹ 9,000; R ₹ 9,000

44. When a new partner brings his share of goodwill in cash, the amount is debited to:

(A) Goodwill A/c
(B) Capital A/c of the new partner
(C) Cash A/c
(D) Capital A/cs of the old partners

45. When a new partner does not bring his share of goodwill in cash, the amount is debited to :

(A) Cash A/c
(B) Premium A/c
(C) Current A/c of the new partner
(D) Capital A/cs of the old partners

46. If, at the time of admission, some profit and loss account balance appears in the books, it will be transferred to :

(A) Profit & Loss Adjustment Account
(B) All partners' Capital Accounts
(C) Old partners' Capital Accounts
(D) Revaluation Account

47. If at the time of admission, there is some unrecorded liability, it will be :

(A) Debited to Revaluation Account
(B) Credited to Revaluation Account
(C) Debited to Goodwill Account
(D) Credited to partners' Capital A/c

48. If the new partner brings his share of goodwill in cash, it will be shared by old partners in :

(A) Ratio of sacrifice
(B) Old profit sharing ratio
(C) New profit sharing ratio
(D) In Capital ratio

HOTS

49. A and B share profits and losses equally. They have ₹20,000 each as capital. They admit C as equal partner and goodwill was valued at ₹30,000. C is to bring in ₹30,000 as his capital and necessary cash towards his share of goodwill. Goodwill Account will not remain open in books. If profit on revaluation is ₹13,000, find the closing balance of the capital accounts.

(A) ₹31,500; ₹31,500; ₹30,000
(B) ₹31,500; ₹31,500; ₹20,000
(C) ₹26,500; ₹26,500; ₹30,000
(D) ₹20,000; ₹20,000; ₹30,000

50. In the absence of an express agreement as to who will contribute to new partners' share of profit, it is implied that the old partners will contribute :

(A) Equally (B) In the ratio of their capitals
(C) In their old profit sharing ratio (D) In the gaining ratio

51. When a new partner brings goodwill in Cash, it is credited to :
(A) His Capital A/c (B) Sacrificing Partner's Capital A/cs
(C) Old Partner's Capital A/cs (D) All Partner's Capital A/cs

52. If the incoming partner brings the amount of goodwill in Cash and also a balance exists in goodwill account, then this goodwill account is written off among the old partners in
(A) The new profit sharing ratio (B) The old profit sharing ratio
(C) The sacrificing ratio (D) The gaining ratio

53. If, at the time of admission, the revaluation A/c shows a profit, it should be credited to :
(A) Old partners capital accounts in the old profit sharing ratio.
(B) All partners capital accounts in the new profit sharing ratio.
(C) Old partners capital accounts in the new profit sharing ratio.
(D) Old partners capital accounts in the sacrificing ratio.

54. Gain / loss on revaluation at the time of change in profit sharing ratio of existing partners is shared by ....(*i*).......... whereas in case of admission of a partner it is shared by .... (*ii*).......... .
(A) (*i*) Remaining Partners, (*ii*) All Partners.
(B) (*i*) All Partners, (*ii*) Old partners.
(C) (*i*) New Partner, (*ii*) All partners.
(D) (*i*) Sacrificing Partner, (*ii*) Incoming partner.
(C.B.S.E. Sample Paper, 2021)

55. Arun and Vijay are partners in a firm sharing profits and losses in the ratio of 5 :1.

Balance Sheet (Extract)

Liabilities	₹	*Assets*	₹
		Machinery	40,000

If the value of machinery reflected in the balance sheet is overvalued by 33⅓ %, find out the value of Machinery to be shown in the new Balance Sheet:
(A) ₹44,000 (B) ₹48,000
(C) ₹32,000 (D) ₹30,000
(C.B.S.E. Sample Paper, 2021)

56. Revaluation Account or Profit and Loss Adjustment A/c is a
(A) Real Account (B) Personal Account
(C) Nominal Account (D) Asset Account

HOTS

57. In case of admission of a partner, the entry for unrecorded investments will be:
(A) Debit Partners Capital A/cs and Credit Investments A/c
(B) Debit Revaluation A/c and Credit Investment A/c

(C) Debit Investment A/c and Credit Revaluation A/c
(D) None of the above

58. When the balance sheet is prepared after the new partnership agreement, the assets and liabilities are recorded at :
(A) Historical cost (B) Current cost
(C) Realisable value (D) Revalued figures

HOTS

59. Goodwill of a firm of *A* and *B* is valued at ₹30,000. It is appearing in the books at ₹12,000. *C* is admitted for 1/4 share. What amount he is supposed to bring for goodwill?
(A) ₹3,000 (B) ₹4,500
(C) ₹7,500 (D) ₹10,500

HOTS

60. *A* and *B* are partners of a partnership firm sharing profits in the ratio of 3 : 2 respectively. *C* was admitted for 1/5th share of profit. Machinery would be appreciated by 10% (book value ₹80,000) and building would be depreciated by 20% (₹2,00,000). Unrecorded debtors of ₹1,250 would be brought into books now and a creditor amounting to ₹2,750 died and need not pay anything on this account. What will be profit/loss on revaluation?
(A) Loss ₹28,000 (B) Loss ₹ 40,000
(C) Profits ₹28,000 (D) Profits ₹40,000

HOTS

61. *X* and *Y* are partners sharing profits in the ratio 5 : 3. They admitted *Z* for 1/5th profits, for which he paid ₹60,000 against capital and ₹30,000 against goodwill. Find the capital balance for each partner taking *Z*'s capital as base capital.
(A) ₹1,50,000; ₹60,000 and ₹60,000 (B) ₹1,50,000; ₹60,000 and ₹90,000
(C) ₹1,50,000; ₹90,000 and ₹60,000 (D) ₹1,50,000; ₹90,000 and ₹90,000

HOTS

62. Ramesh and Suresh are partners sharing profits in the ratio of 2 : 1 respectively. Ramesh Capital is ₹1,02,000 and Suresh Capital is ₹73,000. They admit Mahesh and agree to give him 1/5th share in future profit. Mahesh brings ₹14,000 as his share of goodwill. He agrees to contribute capital in the new profit sharing ratio. How much capital will be brought by Mahesh?
(A) ₹43,750 (B) ₹45,000
(C) ₹47,250 (D) ₹48,000

63. Disha and Abha were partners in a firm. Farad was admitted as a new partner for 1/5th share in the profits of the firm. Farad brought proportionate capital. Capitals of Disha and Abha after all adjustments were ₹64,000 and ₹46,000 respectively. Capital brought by Farad was :
(A) ₹22,000 (B) ₹27,500
(C) ₹55,000 (D) ₹28,000 *(C.B.S.E. 2020, Delhi)*

HOTS

64. *A* and *B* are in partnership sharing profits in the ratio of 3 : 2. They take *C* as a new partner. Goodwill of the firm is valued at ₹3,00,000 and *C* brings ₹30,000 as his share of goodwill in cash which is entirely credited to the Capital Account of *A*. New profit sharing ratio will be :
   (A) 3 : 2 : 1 (B) 6 : 3 : 1
   (C) 5 : 4 : 1 (D) 4 : 5 : 1

HOTS

65. *X* and *Y* are partners sharing profits in the ratio of 4 : 3. Z is admitted for 1/5th share and he brings in ₹1,40,000 as his share of goodwill in cash of which ₹1,20,000 is credited to *X* and remaining amount to *Y*. New profit sharing ratio will be :
   (A) 4 : 3 : 5 (B) 2 : 2 : 1
   (C) 1 : 2 : 2 (D) 2 : 1 : 2

HOTS

66. *A* and *B* are partners sharing profits in the ratio of 2 : 3. Their Balance Sheet shows Machinery at ₹2,00,000; Stock at ₹80,000 and Debtors at ₹1,60,000. *C* is admitted and new profit sharing ratio is agreed at 6 : 9 : 5. Machinery is revalued at ₹1,40,000 and a provision is made for doubtful debts @5%. *A*'s share in loss on revaluation amount to ₹20,000. Revalued value of Stock will be :
   (A) ₹62,000 (B) ₹1,00,000
   (C) ₹60,000 (D) ₹ 98,000

67. Angle and Circle were partners in a firm. Their Balance Sheet showed Furniture at ₹2,00,000; Stock at ₹1,40,000; Debtors at ₹1,62,000 and Creditors at ₹60,000. Square was admitted and new profit-sharing ratio was agreed at 2 :3 :5. Stock was revalued at ₹1,00,000, Creditors of ₹15,000 are not likely to be claimed, Debtors for ₹2,000 have become irrecoverable and Provision for doubtful debts to be provided @ 10%.
   Angle's share in loss on revaluation amounted to ₹30,000. Revalued value of Furniture will be :
   (A) ₹2,17,000 (B) ₹1,03,000
   (C) ₹3,03,000 (D) ₹1,83,000
   (C.B.S.E. Sample Paper, 2021)

68. *A*, *B* and *C* are partners sharing profits in ratio of 3 : 2 : 1. They agree to admit *D* into the firm. *A*, *B* and *C* agreed to give 1/3rd, 1/6th, 1/9th share of their profit. The share of profit of *D* will be :
   (A) $\frac{1}{10}$ (B) $\frac{11}{54}$
   (C) $\frac{12}{54}$ (D) $\frac{13}{54}$

69. *X* and *Y* are partners sharing profits in the ratio 2 : 3. They admitted *Z* for 1/5th share of profits, for which he paid ₹1,20,000 against capital and ₹60,000 as

goodwill. Find the capital balances for each partner taking Z's capital as base capital.

(A) ₹3,00,000, ₹1,20,000 and ₹1,20,000
(B) ₹3,00,000, ₹1,20,000 and ₹1,80,000
(C) ₹1,92,000, ₹2,88,000 and ₹1,20,000
(D) ₹3,00,000, ₹1,80,000 and ₹1,80,000

70. A, B, C and D are partners. A and B share 2/3rd of profits equally and C and D share remaining profits in the ratio of 3 : 2. Find the profit sharing ratio of A, B, C and D.

(A) 5 : 5 : 3 : 2 (B) 7 : 7 : 6 : 4
(C) 2.5 : 2.5 : 8 : 6 (D) 3 : 9 : 8 : 3

71. Sacrificing ratio is used to distribute .... in case of admisstion of a partner :

(A) Reserves (B) Goodwill
(C) Revaluation Profit (D) Balance in Profit and Loss Account

72. X and Y are partners in a firm with capital of ₹1,80,000 and ₹2,00,000. Z was admitted for 1/3rd share in profits and brings ₹3,40,000 as capital, calculate the amount of goodwill :

(A) ₹2,40,000 (B) ₹1,00,000
(C) ₹1,50,000 (D) ₹3,00,000

73. A and B are partners sharing profits and losses in the ratio of 5 : 3. On admission, C brings ₹70,000 as cash and ₹43,000 against Goodwill. New profit ratio between A, B and C is 7 : 5 : 4. The sacrificing ratio of A and B is:

(A) 3 : 1 (B) 1 : 3
(C) 4 : 5 (D) 5 : 9

74. A and B are partners in a firm having capitals of ₹54,000 and ₹36,000 respectively. They admitted C for 1/3rd share in the profits. C brought proportionate amount of capital. The Capital brought in by C would be :

(A) ₹90,000 (B) ₹45,000
(C) ₹54,000 (D) ₹36,000

(C.B.S.E. Sample Paper, 2019)

75. Mona and Tina were partners in a firm sharing profits in the ratio of 3 : 2. Naina was admitted with $\frac{1}{6}$th share in the profits of the firm. At the time of admission, Workmen's Compensation Reserve appeared in the Balance Sheet of the firm at ₹32,000. The claim on account of workmen's compensation was determined at ₹40,000. Excess of claim over the reserve will be :

(A) Credited to Revaluation Account.
(B) Debited to Revaluation Account.
(C) Credited to old partner's Capital Accounts.
(D) Debited to old partner's Capital Accounts.

(C.B.S.E. 2020; Chennai, Mumbai)

76. Sun and Star were partners in a firm sharing profits in the ratio of 2 : 1. Moon was admitted as a new partner in the firm. New profit sharing ratio was 3 : 3 : 2. Moon brought the following assets towards his share of goodwill and his capital :

Machinery ₹2,00,000; Furniture ₹1,20,000; Stock ₹80,000; Cash ₹50,000

If his capital is considered as ₹3,80,000, the goodwill of the firm will be :

(A) ₹70,000
(B) ₹2,80,000
(C) ₹4,50,000
(D) ₹1,40,000

(C.B.S.E. 2020; Chennai, Mumbai)

77. Runa and Ria were partners in a firm sharing profits and losses in the ratio of 3 : 1. On 1st April, 2020, Uday is admitted as a new partner in the firm for 3/8th share in the profits on various terms, one of them being his contribution of ₹42,000 as capital.

The new profit-sharing ratio amongst all the partners to be 3 : 2 : 3.

The capitals of Runa and Ria, after taking into account all the terms of admission were ₹61,625 and ₹25,375.

It is decided that the Capital Accounts of Runa and Ria be adjusted in the ratio of their respective share in the profits after admission, any surplus to be adjusted through the Current Account while any deficiency through the Cash Account.

The surplus capital adjusted through current account will be:

(A) Ria's debit capital balance of ₹2,625
(B) Runa's credit capital balance of ₹2,625
(C) Ria's debit capital balance of ₹19,625
(D) Runa's credit capital balance of ₹19,625

(I.S.C. Sample Paper, 2021)

78. At the time of admission of new partner Vasu, Old partners Paresh and Prabhav had debtors of ₹6,20,000 and a provision for doubtful debts of ₹20,000 in their books. As per terms of admission, assets were revalued, and it was found that debtors worth ₹15,000 had turned bad and hence should be written off. Which journal entry reflects the correct accounting treatment of the above situation.

Date	Particulars		L.F.	Dr. Amount	Cr. Amount
				₹	₹
(A)	Bad Debts A/c	Dr.		15,000	
	To Sundry Debtors				15,000
	Provision for Doubtful Debts A/c	Dr.		15,000	
	To Bad Debts A/c				15,000
(B)	Bad Debt A/c	Dr.		15,000	
	To Sundry Debtors				15,000
	Revaluation A/c	Dr.		15,000	
	To Provision for Doubtful Debts A/c				15,000

(C)	Revaluation A/c	Dr.	15,000	
	To Sundry Debtors A/c			15,000
(D)	Bad Debts A/c	Dr.	15,000	
	To Revaluation A/c			15,000

(C.B.S.E. Sample Paper, 2021)

[See answers at the end of the book]

4

Retirement or Death of a Partner

LEARNING OBJECTIVES

After studying this Chapter you should be able to understand :

- **New Profit-Sharing Ratio and Gaining Ratio**
- **Distinction between Sacrificing Ratio and Gaining Ratio**
- **Accounting Treatment of Goodwill when a Partner Retires or Dies**
- **Accounting Treatment for Revaluation of Assets and Liabilities**
- **Accounting Treatment of Reserves and Accumulated Profits**
- **Adjustment of Capitals according to the New Profit-Sharing Ratio**
- **Disposal of the Amount Due to the Retiring Partner**
- **Calculation of Amount Payable to the Representatives of a Deceased Partner**

Retirement of a Partner

A partner has the right to retire from the firm after giving due notice in advance. Old partnership comes to an end after the retirement of a partner, but the firm continues and a new partnership comes into existence between the remaining partners.

A retiring partner is entitled to get the following :

1. **Share in Goodwill :—** Goodwill of the firm is valued and the retiring partner's share of goodwill is credited to his Capital Account.

2. **Share in Reserves :—** Reserves are the undistributed profits of the previous years. Hence, the retiring partner's share of reserves or undistributed profits is also credited to his Capital Account.

3. **Share in Revaluation of Assets and Liabilities :—** Assets and Liabilities are revalued on the date of retirement and retiring partner's share of profit is credited or the loss is debited to his Capital Account.

4. Share in Reserves, Accumulated profits and losses.

5. Share in surrender value of joint life policy.

Total amount due to the retiring partner, thus ascertained, is either paid off immediately or is transferred to his loan account, to be paid afterwards.

Calculation of New Profit Sharing Ratio

I. If the new profit sharing ratios of the remaining partners are not given in the question, it will be assumed that the remaining partners continue to share profits and losses in the old ratio.

ILLUSTRATION 1.

X, Y and *Z* are partners sharing profits and losses in the ratio of 5 : 4 : 3. Calculate the new ratios when :

(*i*) *X* retires, (*ii*) *Y* retires, (*iii*) *Z* retires.

SOLUTION :

New ratio of the remaining partners will be calculated by striking out the share of the retiring partner. Thus,

(*i*) When *X* retires, the new ratio between *Y* and *Z* is 4 : 3

(*ii*) When *Y* retires, the new ratio between *X* and *Z* is 5 : 3

(*iii*) When *Z* retires, the new ratio between *X* and *Y* is 5 : 4

ILLUSTRATION 2.

A, B and *C* are partners sharing profits in the ratio of 1/2 : 1/3 : 1/6. Find out the new ratio if *B* retires.

SOLUTION :

The ratio of *A, B* and *C* is $\frac{1}{2} : \frac{1}{3} : \frac{1}{6}$.

This can be written as $\frac{3 : 2 : 1}{6}$ or 3 : 2 : 1

∴ If *B* retires, the new ratio between *A* and *C* is 3 : 1

(2) Sometimes the remaining partners purchase the share of retiring partner in some specified proportions. In such cases the fraction of shares purchased by them is added to their old share and the new ratio is calculated.

ILLUSTRATION 3.

A, B and *C* are partners in a firm sharing profits in the ratio of 5 : 4 : 3. *B* retired and his share was divided equally between *A* and *C*. Calculate the new profit sharing ratio of *A* and *C*.

SOLUTION :

B's share will be divided between *A* and *C* in the ratio of 1 : 1.

A will gain $\frac{1}{2}$ of $\frac{4}{12}$ $= \frac{2}{12}$

Hence, *A*'s new share $= \frac{5}{12} + \frac{2}{12} = \frac{7}{12}$

C will gain $\frac{1}{2}$ of $\frac{4}{12}$ $= \frac{2}{12}$

Hence, C's new share $= \frac{3}{12} + \frac{2}{12} = \frac{5}{12}$

New Ratio $= A\frac{7}{12} : C\frac{5}{12}$ or 7 : 5

ILLUSTRATION 4.

A, *B* and *C* were partners sharing profits in the ratio of 5 : 4 : 3. *C* retired and his share was taken up by *A* and *B* in the ratio of 3 : 2. Find out the new ratio.

SOLUTION :

C's share will be divided between *A* and *B* in the ratio of 3 : 2.

A will gain $\frac{3}{5}$ of $\frac{3}{12} = \frac{9}{60}$

Hence, *A*'s new share $= \frac{5}{12} + \frac{9}{60} = \frac{34}{60}$

B will gain $\frac{2}{5}$ of $\frac{3}{12} = \frac{6}{60}$

Hence, *B*'s new share $= \frac{4}{12} + \frac{6}{60} = \frac{26}{60}$

New Ratio $= A\frac{34}{60} : B\frac{26}{60}$ or 17 : 13.

ILLUSTRATION 5.

A, *B* and *C* are partners in a firm sharing profits and losses as $\frac{7}{15}, \frac{1}{3}$ and $\frac{1}{5}$ respectively. *B* retires and his share is taken by *A* and *C* in the ratio of 3 : 2. Immediately, *D* is admitted for $\frac{1}{3}$rd share of profit, $\frac{1}{4}$th of which was given by *A* and the remaining share was taken equally from *A* and *C*. Calculate new profit-sharing ratio after *D*'s admission.

SOLUTION :

	A	*C*
(*i*) Existing Share	$\frac{7}{15}$	$\frac{1}{5}$
(*ii*) Share acquired from *B*	$\frac{1}{3} \times \frac{3}{5} = \frac{1}{5}$	$\frac{1}{3} \times \frac{2}{5} = \frac{2}{15}$
(*iii*) New Share (*i* + *ii*)	$\frac{7}{15} + \frac{1}{5} = \frac{10}{15}$	$\frac{1}{5} + \frac{2}{15} = \frac{5}{15}$

Thus, New Share of *A* and *C* $= \frac{10}{15} : \frac{5}{15}$ or 2 : 1

(*iv*) Share given by *A* to *D* $= \frac{1}{3} \times \frac{1}{4} = \frac{1}{12}$

(*v*) Remaining share to be acquired by *D* $= \frac{1}{3} - \frac{1}{12} = \frac{4-1}{12} = \frac{3}{12}$

It is acquired by D equally from A and C

Thus, D acquires $\frac{1}{2}$ of $\frac{3}{12} = \frac{1}{8}$ each from A and C

(*vi*) New Share of A $= \frac{2}{3} - \frac{1}{12} - \frac{1}{8} = \frac{16-2-3}{24} = \frac{11}{24}$

New Share of C $= \frac{1}{3} - \frac{1}{8} = \frac{8-3}{24} = \frac{5}{24}$

Hence, New Profit Sharing Ratio of A, C and $D = \frac{11}{24} : \frac{5}{24} : \frac{1}{3} = 11 : 5 : 8$

Calculation of Gaining Ratio

Meaning of Gaining Ratio :— It is calculated when a partner retires or dies. When a partner retires or dies, his share of profit is taken over by the remaining partners. The ratio in which the remaining partners share increases is called the gaining ratio. Gaining ratio is the ratio in which the remaining partners will pay the amount of goodwill to the retiring partner.

Calculation of Gaining Ratio :— This ratio is calculated by the following two methods :

1. If the new profit sharing ratios of the remaining partners are not given in the question, it will be assumed that the remaining partners continue to share profits in the old ratio. Thus, gain to the continuing partners is in the old ratio. For example, A, B and C shared profits in the ratio of 5 : 3 : 2. If B retires, his share will be taken by A and C in the ratio of 5 : 2 and the new ratio in future will also be 5 : 2.
2. If the new profit sharing ratio of the remaining partners is given in the question, gaining ratio is calculated by deducting old ratio from the new ratio.

Gaining Ratio = New Ratio – Old Ratio

ILLUSTRATION 6.

X, Y and Z are partners sharing profits and losses in the ratio of 3 : 2 : 1. Calculate the gaining ratio and new ratios when :

(*i*) X retires, (*ii*) Y retires, (*iii*) Z retires.

SOLUTION :

Since the new profit sharing ratio of the remaining partners is not given in the question, it will be assumed that the remaining partners have gained in their old ratio.

(*i*) When X retires, the gaining ratio between Y and Z is 2 : 1.

(*ii*) When Y retires, the gaining ratio between X and Z is 3 : 1.

(*iii*) When Z retires, the gaining ratio between X and Y is 3 : 2.

New ratio of the remaining partners will be calculated by striking out the share of the retiring partner. Thus,

(*i*) When X retires, the new ratio between Y and Z is 2 : 1.

(*ii*) When Y retires, the new ratio between X and Z is 3 : 1.

(*iii*) When Z retires, the new ratio between X and Y is 3 : 2.

ILLUSTRATION 7.

A, *B* and *C* are partners sharing profits and losses in the ratio of 4 : 3 : 2. *B* retires. *A* and *C* decided to share the profits and losses in future in the ratio of 5 : 4. Calculate gaining ratio.

SOLUTION :

Gaining Ratio = New Ratio – Old Ratio

$\therefore$ *A*'s Gaining ratio $= \frac{5}{9} - \frac{4}{9} = \frac{1}{9}$

C's Gaining Ratio $= \frac{4}{9} - \frac{2}{9} = \frac{2}{9}$

$\therefore$ Gaining Ratio between *A* and *C* $= \frac{1}{9} : \frac{2}{9}$ or 1 : 2.

Distinction Between Sacrificing Ratio and Gaining Ratio

Sacrificing ratio is the ratio of decrease in the old partner's share of profits at the time of admission of a new partner, whereas the Gaining ratio is the ratio of gain in the remaining partner's share of profits at the time of retirement or death of a partner.

There are following differences between the two :

Basis of Difference	Sacrificing Ratio	Gaining Ratio
1. **Meaning**	It is the ratio in which the old partners surrender a part of their share in favour of new partner.	It is the ratio in which the remaining partners acquire the outgoing (retired or deceased) partner's share.
2. **When Calculated**	Sacrificing ratio is calculated at the time of the admission of a new partner.	Gaining ratio is calculated at the time of the retirement or death of a partner.
3. **Formula for Calculation**	Formula for calculating this ratio is as follows : Sacrificing Ratio = Old Ratio — New Ratio	Formula for calculating this ratio is as follows : Gaining Ratio = New Ratio — Old Ratio
4. **Purpose of Calculation**	New partner's share of goodwill is divided between the old partners in sacrificing ratio.	Goodwill paid to retiring partner is paid by the remaining partners in their gaining ratio.

Accounting Treatment of Goodwill

The retiring or deceased partner is entitled to his share of goodwill at the time of retirement or death because the goodwill earned by the firm is the result of the efforts of all the existing partners in the past. Since a part of the future profits will be accruing because of the present goodwill and the retiring or deceased partner will not be sharing future profits, it will be fair to compensate the retiring or deceased partner for the same. At the time of retirement or death of a partner, the goodwill is evaluated on the basis of agreement among the partners (as discussed in Chapter 2).

As already discussed in the previous chapter, Accounting Standard 26 (Ind AS-38) specifies that goodwill can be recorded in the books only when some consideration in

money or money's worth has been paid for it. Hence, only purchased goodwill can be recorded in the books and the **Goodwill Account cannot be raised.**

As such, in case of retirement or death of a partner, the adjustment for goodwill will be made through partner's capital accounts. The retiring or deceased partner's capital account will be credited with his share of goodwill and continuing partner's capital accounts will be debited in their gaining ratio. The following journal entry will be recorded :

Continuing Partner's Capital A/cs	Dr.	(in the gaining ratio)
To Retiring / Deceased Partner's Capital A/c		(with his share of goodwill)
(Retiring/deceased partner's share of goodwill adjusted to continuing partners in the gaining ratio)		

ILLUSTRATION 8.

P, *Q* and *R* are partners sharing profits in the ratio of 7 : 5 : 4. *R* retires and the goodwill of the firm is valued at ₹1,60,000. No goodwill account appears as yet in the books of the firm. *P* and *Q* will share future profits equally. Pass necessary journal entry for goodwill.

SOLUTION : JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	P's Capital A/c	Dr.		10,000	
	Q's Capital A/c	Dr.		30,000	
	To *R*'s Capital A/c				40,000
	(Retiring partner's share of goodwill adjusted to remaining partners in their gaining ratio 1 : 3)				

Note : Gaining Ratio = New Ratio – Old Ratio

P Gains $= \frac{1}{2} - \frac{7}{16} = \frac{8-7}{16} = \frac{1}{16}$

Q Gains $= \frac{1}{2} - \frac{5}{16} = \frac{8-5}{16} = \frac{3}{16}$

As such, gaining ratio between *P* and *Q* = 1 : 3

When the Goodwill Account is already appearing in the books :

Usually, the goodwill is not shown in the books of a firm. However, if, at the time of retirement or death of a partner, it appears in the balance sheet of a firm, it will be written off by debiting all the partner's capital accounts in their old profit sharing ratio and crediting the goodwill account. In such a case, the following journal entry is recorded :

All Partner's Capital A/cs	Dr.	(in old ratio)
To Goodwill A/c		(goodwill existing in the books)
(Goodwill existing in the books written off)		

ILLUSTRATION 9.

A, *B* and *C* are sharing profits in the ratio of 3 : 2 : 1. Goodwill is appearing in the books at a value of ₹2,40,000. *B* retires and on the day of *B*'s retirement Goodwill is

valued at ₹6,00,000. A and C decided to share future profits in the ratio of 3 : 2. Pass the necessary Journal entries.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	A's Capital A/c	Dr.		1,20,000	
	B's Capital A/c	Dr.		80,000	
	C's Capital A/c	Dr.		40,000	
	To Goodwill A/c				2,40,000
	(Goodwill existing in the books written off in old ratio)				
	A's Capital A/c	Dr.		60,000	
	C's Capital A/c	Dr.		1,40,000	
	To B's Capital A/c (2/6 of 6,00,000)				2,00,000
	(B's share of goodwill adjusted to remaining partners in their gaining ratio 3 : 7)				

Note : Gaining Ratio = New Ratio – Old Ratio

$$A \text{ Gains} = \frac{3}{5} - \frac{3}{6} = \frac{18-15}{30} = \frac{3}{30}$$

$$C \text{ Gains} = \frac{2}{5} - \frac{1}{6} = \frac{12-5}{30} = \frac{7}{30}$$

As such Gaining Ratio between A and C = 3 : 7

ILLUSTRATION 10.

Apurva, Dimple, Komal and Saloni are partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1 : 1. Dimple and Komal decided to retire from the firm. The goodwill of the firm was valued at ₹9,00,000. Apurva and Saloni decided to share future profits and losses in the ratio of 3 : 2.

Pass necessary journal entry for the treatment of goodwill.

SOLUTION :

Calculation of Gaining Ratio :

$$\text{Apurva Gains} = \frac{3}{5} - \frac{2}{6} = \frac{18-10}{30} = \frac{8}{30}$$

$$\text{Saloni Gains} = \frac{2}{5} - \frac{1}{6} = \frac{12-5}{30} = \frac{7}{30}$$

As such Gaining Ratio between Apurva and Saloni = 8 : 7

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Apurva's Capital A/c (8/15 of ₹4,50,000)(1)	Dr.		2,40,000	
	Saloni's Capital A/c (7/15 of ₹4,50,000)	Dr.		2,10,000	
	To Dimple's Capital A/c				3,00,000
	To Komal's Capital A/c				1,50,000
	(Dimple and Komal's share of goodwill debited to the gaining partners in their gaining ratio of 8 : 7)				

Working Note :

		₹
(1) Dimple's Share of Goodwill= ₹9,00,000 × $\frac{2}{6}$	=	3,00,000
Komal's Share of Goodwill = ₹9,00,000 × $\frac{1}{6}$	=	1,50,000
		4,50,000

ILLUSTRATION 11.

A, B, C and *D* are partners sharing profits in the ratio of 3 : 4 : 3 : 2. On the retirement of *C*, the goodwill was valued at ₹6,00,000. *A, B* and *D* decided to share future profits equally. Pass the necessary journal entry for the treatment of goodwill.

SOLUTION :

Calculation of Gaining Ratio :

Gaining Ratio of *A* $= \frac{1}{3} - \frac{3}{12} = \frac{4-3}{12} = \frac{1}{12}$

Gaining Ratio of *B* $= \frac{1}{3} - \frac{4}{12} = \frac{4-4}{12} = 0$

Gaining Ratio of *D* $= \frac{1}{3} - \frac{2}{12} = \frac{4-2}{12} = \frac{2}{12}$

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	A's Capital A/c	Dr.		50,000	
	D's Capital A/c	Dr.		1,00,000	
	To *C*'s Capital A/c				1,50,000
	(*C*'s share of goodwill debited to the accounts of *A* and *D* in the gaining ratio 1 : 2)				

ILLUSTRATION 12.

A, B, C, D and *E* were partners in a firm sharing profits and losses in the ratio of 5 : 4 : 3 : 2 : 1 respectively. Unfortunately, *D* and *E* met with a tragic car accident in which both of them died on the spot.

The goodwill of the firm was valued at ₹1,50,000 and *A, B* and *C* decided to share future profits and losses in the ratio of 4 : 6 : 5 respectively.

Give Journal entry for goodwill.

SOLUTION :

	A	*B*	*C*	*D*	*E*
Old Ratio	5/15	4/15	3/15	2/15	1/15
(–) New Ratio	4/15	6/15	5/15	–	–
Sacrifice or Gain	1/15	2/15	2/15	2/15	1/15
	Sacrifice	Gain	Gain	Sacrifice	Sacrifice

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	B's Capital A/c (2/15 of 1,50,000)	Dr.		20,000	
	C's Capital A/c (2/15 of 1,50,000)	Dr.		20,000	
	To A's Capital A/c (1/15 of 1,50,000)				10,000
	To D's Capital A/c (2/15 of 1,50,000)				20,000
	To E's Capital A/c (1/15 of 1,50,000)				10,000
	(Adjustment entry for goodwill on the death of D and E)				

ILLUSTRATION 13.

A, B and *C* are partners sharing profits and losses in the ratio of 4 : 3 : 1 respectively. *B* retires, selling his share of profit to *A* and *C* for ₹81,000; ₹36,000 being paid by *A* and ₹45,000 by *C*. The profit for the year after *B*'s retirement was ₹1,05,000.

You are required (*i*) to give necessary journal entries to record the above said sale of *B*'s share to *A* and *C*, (*ii*) to calculate the new profit sharing ratio, and (*iii*) distribute the profit between *A* and *C*.

SOLUTION : (i) JOURNAL ENTRIES

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	A's Capital A/c	Dr.		36,000	
	C's Capital A/c	Dr.		45,000	
	To B's Capital A/c				81,000
	(Sale of B's share to A and C for ₹81,000)				
	Profit and Loss Appropriation A/c	Dr.		1,05,000	
	To A's Capital A/c				70,000
	To C's Capital A/c				35,000
	(Profit distributed after B's retirement in their new ratio *i.e.*, 2 : 1)				

(*ii*) Calculation of new profit sharing ratio :

A and *C* purchased *B*'s share for ₹81,000, out of which *A* pays ₹36,000 and *C* pays ₹45,000, *i.e.*, *A* and *C* will share *B*'s share of profit in the ratio of 36,000 : 45,000 = 4 : 5.

As such, new profit sharing ratios of *A* and *C* will be :

A gets $\frac{4}{9}$ th of *B*'s share of $\frac{3}{8} = \frac{4}{9} \times \frac{3}{8} = \frac{12}{72}$

A's old share $= \frac{4}{8}$

$\therefore$ *A*'s new share $= \frac{4}{8} + \frac{12}{72} = \frac{36+12}{72} = \frac{48}{72} = \frac{2}{3}$

C gets $\frac{5}{9}$ th of *B*'s share of $\frac{3}{8} = \frac{5}{9} \times \frac{3}{8} = \frac{15}{72}$

C's old share $= \frac{1}{8}$

$\therefore$ C's new share $= \frac{1}{8} + \frac{15}{72} = \frac{9+15}{72} = \frac{24}{72} = \frac{1}{3}$

Hence, New ratio between A and $C = \frac{2}{3} : \frac{1}{3} = 2:1$

(iii) Division of Profit between A and C :

New Profit sharing ratio between A and C $= 2:1$

Profit $=$ ₹1,05,000

A's share $=$ ₹1,05,000 $\times \frac{2}{3} =$ ₹70,000;

C's share $=$ ₹1,05,000 $\times \frac{1}{3} =$ ₹35,000.

Revaluation of Assets and Liabilities

At the time of retirement the assets and liabilities are revalued and a revaluation account is prepared in the same way as is done in case of admission of a new partner. The only difference is that in case of retirement any profit or loss due to revaluation is divided among all the partners, including the retiring partner, whereas in case of admission of a new partner, the new partner does not share such profit or loss on revaluation.

Adjustment of Accumulated Profits and Reserves :

If at the time of retirement there is any balance of General Reserve, Reserve Fund or any undistributed amount of P & L A/c appearing in the Balance Sheet, it belongs to all the partners and should be transferred to the capital accounts of all partners' in their old profit sharing ratio. Following entries are passed for this purpose :

(*i*) For distributing Reserves and Accumulated Profits :

General Reserves A/c Dr.
Reserve Fund A/c Dr.
Profit & Loss A/c (Credit balance) Dr.
To All Partner's Capital A/cs or Current A/cs (in old ratio)

(*ii*) For distributing accumulated losses :

All Partner's Capital A/cs or Current A/cs Dr. (in old ratio)
To Profit & Loss A/c (Debit balance)

(*iii*) For distributing surplus of Specific Reserves :

In case specific reserves like 'Workmen's Compensation Reserve' or 'Investment Fluctuation Reserve' are in excess of actual obligations, the excess will be transferred to capital accounts of all partners in old ratio. The entry will be :

Workmen's Compensation Reserve A/c Dr.
Investment Fluctuation Reserve A/c Dr.
To All Partner's Capital A/cs or Current A/cs (in old ratio)

ILLUSTRATION 14.

A, *B* and *C* are partners in a firm sharing profits in the ratio of 2 : 3 : 4. On 31st March 2022, *A* retires and *B* and *C* decided to share future profits in the ratio of 2 : 1. Following balances appeared in their books on this date :

	₹
Profit and Loss (Dr.)	72,000
Employee's Provident Fund	1,50,000
Workmen Compensation Reserve	45,000
General Reserve	1,20,000

It is agreed that (*i*) workmen Compensation Reserve is no more required, and (*ii*) 25% of the General Reserve is to be transferred to Provision for Doubtful Debts.

Pass journal entries for the adjustment of these items on *A*'s retirement.

SOLUTION :

Books of *A*, *B* and *C*

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022 March 31	*A*'s Capital A/c	Dr.		16,000	
	B's Capital A/c	Dr.		24,000	
	C's Capital A/c	Dr.		32,000	
	To Profit and Loss A/c				72,000
	(Accumulated loss transferred to the capital accounts of all partners in old ratio on *A*'s retirement)				
	Workmen Compensation Reserve A/c	Dr.		45,000	
	To *A*'s Capital A/c				10,000
	To *B*'s Capital A/c				15,000
	To *C*'s Capital A/c				20,000
	(Workmen Compensation Reserve transferred to Capital Accounts in old ratio on *A*'s retirement)				
	General Reserve A/c	Dr.		1,20,000	
	To Provision for Doubtful Debts A/c				30,000
	To *A*'s Capital A/c				20,000
	To *B*'s Capital A/c				30,000
	To *C*'s Capital A/c				40,000
	(25% of General Reserve transferred to Provision for Doubtful Debts and balance transferred to Capital Accounts in old ratio)				

Note : Employee's Provident Fund is an outside liability and is not an accumulated profit. As such, it is not distributed among the partners.

ILLUSTRATION 15.

A, *B* and *C* are partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. *C* retires from the firm and *A* and *B* agree to share future profits equally. Give journal entries on *C*'s retirement in the following cases :

(*a*) Workmen Compensation Reserve appears in the books at ₹1,00,000, when there is a claim of ₹40,000 against it.

(*b*) Workmen Compensation Reserve appears in the books at ₹2,00,000, when there is a claim of ₹2,75,000 against it.

(*c*) Investment Fluctuation Reserve appears in the books at ₹50,000, when Investments (market value ₹1,80,000) appear at ₹2,00,000.

(*d*) Investment Fluctuation Reserve appears in the books at ₹20,000, when Investments (market value ₹1,20,000) appear at ₹2,00,000.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
(*a*)	Workmen Compensation Reserve A/c	Dr.		1,00,000	
	To Provision for Workmen Compensation Claim A/c				40,000
	To *A*'s Capital A/c				30,000
	To *B*'s Capital A/c				20,000
	To *C*'s Capital A/c				10,000
	(Surplus workmen compensation reserve credited to old Partners' Capital Accounts in their old profit-sharing ratio)				
(*b*)	Workmen Compensation Reserve A/c	Dr.		2,00,000	
	Revaluation A/c	Dr.		75,000	
	To Provision for Workmen Compensation Claim A/c				2,75,000
	(Provision made for workmen claim and shortfall charged to Revaluation Account)				
	A's Capital A/c	Dr.		37,500	
	B's Capital A/c	Dr.		25,000	
	C's Capital A/c	Dr.		12,500	
	To Revaluation A/c				75,000
	(Loss on revaluation debited to Partners' Capital Accounts in their old profit-sharing ratio)				
(*c*)	Investment Fluctuation Reserve A/c	Dr.		50,000	
	To Investments A/c				20,000
	To *A*'s Capital A/c				15,000
	To *B*'s Capital A/c				10,000
	To *C*'s Capital A/c				5,000
	(Excess investment fluctuation reserve credited to Partners' Capital Accounts in their old profit-sharing ratio)				
(*d*)	Investment Fluctuation Reserve A/c	Dr.		20,000	
	Revaluation A/c	Dr.		60,000	
	To Investments A/c				80,000
	(Fall in book value of investments debited to investment fluctuation reserve account and excess fall debited to Revaluation Account)				

A's Capital A/c	Dr.	30,000	
B's Capital A/c	Dr.	20,000	
C's Capital A/c	Dr.	10,000	
To Revaluation A/c			60,000
(Loss on revaluation debited to partners' Capital Accounts in their old profit-sharing ratio)			

Payment of the amount due to retiring partner

When the amount due to the retiring partner is ascertained after all adjustments, it is either paid out in cash or transferred to his loan account.

(*i*) If the amount is paid in cash or by cheque :

Retiring Partner's Capital A/c Dr.
To Cash/Bank
(His share paid off)

(*ii*) If the amount is not paid in cash, the amount due to him will be transferred to his loan account :

Retiring Partner's Capital A/c Dr.
To Retiring Partner's Loan A/c
(Balance of his Capital A/c transferred to his loan A/c)

The amount of loan is repaid to him according to the terms of the agreement. But in the absence of an agreement one has to be guided by Section 37 of the Indian Partnership Act 1932. As per this section the retiring partner is entitled to interest @ 6% p.a. till the loan is paid off. At his option, instead of the interest, he may take that share of profits which has been earned by the firm by the use of the amount due to him. The right is also available to the legal representatives of the deceased partner.

Note : If nothing is mentioned in the question about the payment of the amount due to retiring partner, it will be transferred to his loan account.

ILLUSTRATION 16.

A, *B* and *C* were partners sharing profits and losses in the ratio of 5 : 3 : 2. Their Balance Sheet as at 1st April, 2022 was as follows :

Liabilities		₹	*Assets*	₹
Sundry Creditors		10,000	Cash	2,000
Employee's Provident Fund		5,000	Sundry Debtors	8,000
Reserve Fund		6,000	Stock	40,000
Workmen's Compensation Reserve		2,000	Furniture	13,000
			Patents	4,000
Capitals :			Buildings	60,000
A	50,000		Goodwill	6,000
B	35,000			
C	25,000	1,10,000		
		1,33,000		1,33,000

C retires on above date and the partners agreed that :

(1) Goodwill is to be valued at two year's purchase of the average profits of last four years. Profits for the years ending 31st March were : 2019 : ₹14,400, 2020 : ₹20,000, 2021 : ₹10,000 (Loss), 2022 : ₹15,600.

(2) 5% provision for doubtful debts to be made on debtors.

(3) Stock be appreciated by 10%.

(4) Patents are valueless.

(5) Buildings be appreciated by 20%.

(6) Sundry Creditors to be paid ₹2,000 more than the book value.

Pass Journal entries and prepare Revaluation Account, Capital Accounts and the Balance Sheet of the new firm.

SOLUTION:

JOURNAL ENTRIES

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
April 1	Reserve Fund A/c	Dr.		6,000	
	To *A*'s Capital A/c				3,000
	To *B*'s Capital A/c				1,800
	To *C*'s Capital A/c				1,200
	(The transfer of Reserve Fund to Partner's Capital A/cs in their old profit sharing ratio)				
	Workmen's Compensation Reserve A/c	Dr.		2,000	
	To *A*'s Capital A/c				1,000
	To *B*'s Capital A/c				600
	To *C*'s Capital A/c				400
	(The transfer of Workmen's Compensation Reserve to Partner's Capital A/cs in their old profit sharing ratio)				
	Revaluation A/c	Dr.		6,400	
	To Provision for Doubtful Debts A/c				400
	To Patents A/c				4,000
	To Sundry Creditors A/c				2,000
	(Decrease in the value of assets and increase in creditors)				
	Stock A/c	Dr.		4,000	
	Building A/c	Dr.		12,000	
	To Revaluation A/c				16,000
	(Increase in the value of Assets)				
	Revaluation A/c	Dr.		9,600	
	To *A*'s Capital A/c				4,800
	To *B*'s Capital A/c				2,880
	To *C*'s Capital A/c				1,920
	(Profit on revaluation transferred to partner's Capital A/c)				

A's Capital A/c Dr. *B*'s Capital A/c Dr. *C*'s Capital A/c Dr. To Goodwill A/c (Goodwill appearing in the books written off on *C*'s retirement)		3,000 1,800 1,200	 6,000
A's Capital A/c Dr. *B*'s Capital A/c Dr. To *C*'s Capital A/c (*C*'s share of Goodwill adjusted to the accounts of continuing partners in their gaining ratio 5 : 3)		2,500 1,500	 4,000
C's Capital A/c Dr. To *C*'s Loan A/c (The Balance of *C*'s Capital A/c transferred to *C*'s loan A/c)		31,320	 31,320

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Provision for Doubtful Debts A/c		400	By Stock A/c	4,000
To Patents A/c		4,000	By Buildings A/c	12,000
To Sundry Creditors A/c		2,000		
To Profit transferred to				
A's Capital A/c	4,800			
B's Capital A/c	2,880			
C's Capital A/c	1,920	9,600		
		16,000		16,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Goodwill A/c	3,000	1,800	1,200	By Balance b/d	50,000	35,000	25,000
To *C*'s Capital A/c	2,500	1,500		By Reserve Fund A/c	3,000	1,800	1,200
To *C*'s Loan A/c			31,320	By Workmen's Compensation Reserve A/c	1,000	600	400
To Balance c/d	53,300	36,980		By Revaluation A/c	4,800	2,880	1,920
				By *A*'s Capital A/c			2,500
				By *B*'s Capital A/c			1,500
	58,800	40,280	32,520		58,800	40,280	32,520

BALANCE SHEET OF NEW FIRM (of *A* and *B*)
as at 1st April, 2022

Liabilities	₹	*Assets*		₹
Sundry Creditors	12,000	Cash		2,000
C's Loan	31,320	Sundry Debtors	8,000	

Employee's Provident Fund		5,000	*Less* : Provision for Doubtful Debts	400	7,600
Capitals :			Stock		44,000
A	53,300		Furniture		13,000
B	36,980	90,280	Buildings		72,000
		1,38,600			1,38,600

Working Notes : 1. Calculation of Goodwill : Total profits of the last four years

= ₹14,400 + ₹20,000 – ₹10,000 + ₹15,600 = ₹40,000

Average profit $= ₹\frac{40,000}{4} = ₹10,000$

Goodwill = 10,000 × 2 = ₹20,000

2. In the absence of any information, the retiring partner's balance of Capital Account is transferred to his Loan Account.

3. Amount of Employee's Provident Fund belongs to the employees of the Firm. It will be paid to them on their retirement, hence it cannot be transferred to the Capital Accounts of partners.

ILLUSTRATION 17.

Ram, Shyam and Mohan were in partnership sharing profits and losses in the proportions of 3 : 2 : 1. On 1st April, 2022, Shyam retires from the firm. At that date, their Balance Sheet was as follows :

Liabilities		₹	*Assets*		₹
Trade Creditors		30,000	Cash in Hand		90,000
Bills Payable		27,000	Debtors	1,60,000	
Expenses owing		45,000	*Less* : Provision	10,000	1,50,000
Reserve Fund		1,05,000	Stock		1,20,000
Workmen's Compensation			Factory Premises		2,25,000
Reserve		48,000	Investments		80,000
Capitals :			Loose Tools		40,000
Ram	2,00,000				
Shyam	1,50,000				
Mohan	1,00,000	4,50,000			
		7,05,000			7,05,000

The terms were :

(1) Goodwill of the firm to be valued at 2 times of Average Super Profits of last three years. Taking into consideration the risk of the business, normal profits of the firm are estimated at ₹5,00,000 every year. But actual profits of last three years ending 31st March were as 2020 — ₹6,00,000, 2021 — ₹5,50,000, 2022 — ₹5,75,000.

(2) Expenses owing to be brought down to ₹37,500.

(3) Investments are revalued at ₹72,000. Ram took over investments at this value.

(4) Factory premises is to be revalued at ₹2,43,000; and Loose tools at ₹36,000.

(5) Provision for doubtful Debts to be increased by ₹19,500.

(6) Claim on account of Workmen's Compensation is ₹18,000.

(7) Shyam be paid ₹50,000 in cash and balance due to him treated as a loan carrying interest @ 6% per annum.

Show Journal entry for goodwill adjustment, prepare necessary ledger accounts and opening balance sheet of the continuing partners.

SOLUTION: JOURNAL ENTRY FOR GOODWILL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Ram's Capital A/c	Dr.		37,500	
	Mohan's Capital A/c	Dr.		12,500	
	To Shyam's Capital A/c				50,000
	(Shyam's share of goodwill adjusted to the accounts of continuing partners in their gaining ratio 3 : 1)				

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	Particulars		₹
To Investments	8,000	By Expenses owing A/c		7,500
To Loose Tools	4,000	By Factory Premises		18,000
To Provision for doubtful debts	19,500	By Loss transferred to :		
		Ram's Capital A/c	3,000	
		Shyam's Capital A/c	2,000	
		Mohan's Capital A/c	1,000	6,000
	31,500			31,500

Dr. CAPITAL ACCOUNTS Cr.

Particulars	Ram ₹	Shyam ₹	Mohan ₹	Particulars	Ram ₹	Shyam ₹	Mohan ₹
To Revaluation A/c	3,000	2,000	1,000	By Balance b/d	2,00,000	1,50,000	1,00,000
To Shyam's Capital A/c	37,500	—	12,500	By Reserve fund A/c	52,500	35,000	17,500
To Investment A/c	72,000	—	—	By Workmen's Compensation Reserve A/c	15,000	10,000	5,000
To Cash A/c	—	50,000	—	By Ram's Capital A/c		37,500	
To Shyam's loan A/c	—	1,93,000	—	By Mohan's Capital A/c		12,500	
To Balance c/d	1,55,000	—	1,09,000				
	2,67,500	2,45,000	1,22,500		2,67,500	2,45,000	1,22,500

BALANCE SHEET *as at 1st April, 2022*

Liabilities	₹	Assets		₹
Trade Creditors	30,000	Cash in hand		40,000
Bills Payable	27,000	Debtors	1,60,000	
Expenses Owing	37,500	*Less* : Provision	29,500	1,30,500

			Stock		1,20,000
Liability for Workmen's Compensation Claim		18,000	Factory Premises		2,43,000
Shyam's Loan		1,93,000	Loose Tools		36,000
Capitals :					
Ram	1,55,000				
Mohan	1,09,000	2,64,000			
		5,69,500			5,69,500

Working Notes : Calculation of Goodwill :

Average profits of the past three years $= ₹\frac{6,00,000 + 5,50,000 + 5,75,000}{3}$

$= ₹5,75,000$

Super profits = Actual Profits – Normal Profits

$= ₹5,75,000 - ₹5,00,000 = ₹75,000$

Goodwill at 2 years' purchase of Super Profits $= ₹75,000 \times 2 = ₹1,50,000$

ILLUSTRATION 18.

A, *B* and *C* were partners in a firm. Their Balance Sheet as at 31st March 2019 was as follows :

BALANCE SHEET OF *A*, *B* AND *C*
as at 31st March, 2019

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Bills Payable		20,000	Bank		20,000
Creditors		40,000	Furniture		28,000
General Reserve		30,000	Stock		20,000
Workmen Compensation Reserve		6,000	Sundry Debtors	45,000	
Capitals :			*Less* : Provision for		
A	60,000		Doubtful Debts	5,000	40,000
B	40,000		Land and Building		1,20,000
C	32,000	1,32,000			
		2,28,000			2,28,000

B retired on 1st April, 2019. *A* and *C* decided to share profits in the ratio of 2 : 1. The following terms were agreed upon :

(*i*) Goodwill of the firm was valued at ₹30,000.

(*ii*) Bad-debts ₹4,000 were written off. The provision for doubtful debts was to be maintained @ 10% on debtors.

(*iii*) Land and Building was to be increased to ₹1,32,000.

(*iv*) Furniture was sold for ₹20,000 and payment was received by cheque.

(*v*) Liability towards Workmen Compensation was estimated at ₹1,500.

(*vi*) *B* was to be paid ₹20,000 through a cheque and the balance was transferred to his loan account.

Prepare necessary journal entries. *(C.B.S.E. 2020, Punjab)*

SOLUTION:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019 April 1	General Reserve A/c	Dr.		30,000	
	To *A*'s Capital A/c				10,000
	To *B*'s Capital A/c				10,000
	To *C*'s Capital A/c				10,000
	(General Reserve Credited to partner's Capital A/cs in old ratio *i.e.*, equally)				
,,	Workmen Compensation Reserve	Dr.		6,000	
	To Workmen Compensation Claim A/c				1,500
	To *A*'s Capital A/c				1,500
	To *B*'s Capital A/c				1,500
	To *C*'s Capital A/c				1,500
	(Excess Workmen Compensation Reserve Credited to partner's Capital A/cs in old ratio)				
,,	*A*'s Capital A/c(1)	Dr.		10,000	
	To *B*'s Capital A/c				10,000
	(Adjustment for goodwill)				
,,	Bad Debts A/c	Dr.		4,000	
	To Sundry Debtors A/c				4,000
	(Bad debts written off)				
,,	Provision for Doubtful Debts A/c	Dr.		4,000	
	To Bad Debts A/c				4,000
	(Bad debts adjusted against provision for doubtful debts)				
,,	Revaluation A/c(2)	Dr.		3,100	
	To Provision for Doubtful Debts A/c				3,100
	(Provision created for doubtful debts)				
,,	Land & Building A/c	Dr.		12,000	
	To Revaluation A/c				12,000
	(Increase in the value of land and building)				
,,	Bank A/c	Dr.		20,000	
	Revaluation A/c	Dr.		8,000	
	To Furniture A/c				28,000
	(Furniture sold)				
,,	Revaluation A/c	Dr.		900	
	To *A*'s Capital A/c				300
	To *B*'s Capital A/c				300
	To *C*'s Capital A/c				300
	(Transfer of profit on revaluation)				
,,	*B*'s Capital A/c	Dr.		61,800	
	To Bank A/c				20,000
	To *B*'s Loan A/c				41,800
	(Payment made to *B* and balance transferred to his Loan A/c)				

Working Notes :

(1) Calculation of Gaining Ratio : New Ratio – Old Ratio

$A = \frac{2}{3} - \frac{1}{3} = \frac{1}{3}$ Gain

$B = \frac{1}{3} - \frac{1}{3} =$ Nil

Since A alone has gained, his Capital Account will be debited by B's share of goodwill.

		₹
(2) Net Debtors : ₹45,000 – Bad Debts ₹4,000	=	41,000
Provision @ 10% on ₹41,000		4,100
Less : Existing Provision : ₹5,000 – Bad Debts ₹4,000		1,000
Amount Debited to Revaluation Account		3,100

(3) Net amount payable to B may be ascertained by preparing B's Capital A/c :

Dr. B'S CAPITAL A/C Cr.

Particulars	*Amount*	*Particulars*	*Amount*
	₹		₹
To Bank A/c	20,000	By Balance b/d	40,000
To B's Loan A/c		By General Reserve	10,000
(Balancing Figure)	41,800	By Workmen Compensation Reserve	1,500
		By A's Capital A/c (Goodwill)	10,000
		By Revaluation A/c	300
	61,800		61,800

ILLUSTRATION 19.

D, R and L were in partnership sharing profits and losses in the ratio of 3 : 2 : 1. The draft Balance Sheet as at 31st March, 2022 was as follows :

Liabilities		₹	*Assets*		₹
Capital A/cs :			Building		12,000
D	24,000		Plant and Equipment		18,800
R	12,000		Stock		9,200
L	6,000	42,000	Debtors	12,400	
Current A/cs :			*Less* : Provision for		
D	1,920		Doubtful Debts	1,200	11,200
R	1,680		Balance at Bank		16,120
L	1,120	4,720			
Loan — D		5,000			
Creditors		15,600			
		67,320			67,320

D retired on 31st March, 2022 and R and L continued in partnership, sharing profits and losses in the ratio of 2 : 1. D's loan was repaid on 1st April, 2022 and it was agreed that the remaining balance due to him, other than of the Current Account, should remain as loan to the partnership.

For the purpose of D's retirement, it was agreed that :

(*i*) Building be revalued at ₹24,000 and the Plant and Equipment at ₹15,800.

(*ii*) Provision for Doubtful Debts was to be increased by ₹400.

(*iii*) A provision of ₹500 included in Creditors was no longer required.

(*iv*) ₹1,200 was to be written off the stock in respect of damaged items included threin.

(*v*) A provision of ₹4,240 be made in respect of the outstanding legal charges.

(*vi*) The Goodwill of the firm to be valued at ₹14,400.

You are required to prepare Revaluation Account, Capital and Current Accounts of the partners (assuming all adjustments are to be made through the Current Accounts) and the Balance Sheet of R and L as at 1st April, 2022.

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Plant and Equipment A/c		3,000	By Building A/c	12,000
To Provision for Doubtful Debts A/c		400	By Creditors A/c	500
To Stock A/c		1,200		
To Outstanding Legal Charges A/c		4,240		
To Profit on Revaluation transferred to :				
D's Capital A/c (3/6)	1,830			
R's Capital A/c (2/6)	1,220			
L's Capital A/c (1/6)	610	3,660		
		12,500		12,500

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	D	R	L	*Particulars*	D	R	L
	₹	₹	₹		₹	₹	₹
To D's Loan A/c	24,000	—	—	By Balance b/d	24,000	12,000	6,000
To Balance c/d	—	12,000	6,000				
	24,000	12,000	6,000		24,000	12,000	6,000
				By Balance b/d		12,000	6,000

Dr. PARTNERS' CURRENT ACCOUNTS Cr.

Particulars	D	R	L	*Particulars*	D	R	L
	₹	₹	₹		₹	₹	₹
To D's Current A/c (Goodwill)	—	4,800	2,400	By Balance b/d	1,920	1,680	1,120
				By Revaluation A/c	1,830	1,220	610
To Bank A/c	10,950	—	—	By R's Current			

				A/c (Goodwill)	4,800	—	—
				By *L*'s Current A/c (Goodwill)	2,400	—	—
				By Balance c/d	—	1,900	670
	10,950	4,800	2,400		10,950	4,800	2,400

BALANCE SHEET OF *R* AND *L*

as at 1st April, 2022

Liabilities		₹	*Assets*		₹
Capital Accounts :			Building		24,000
R	12,000		Plant and Equipment		15,800
L	6,000	18,000	Stock		8,000
D's Loan		24,000	Debtors	12,400	
Creditors		15,100	*Less* : Provision for		
Outstanding Legal Charges		4,240	Doubtful Debts	1,600	10,800
			Balance at Bank		
			(₹16,120 – 5,000 – 10,950)		170
			Current A/cs :		
			R	1,900	
			L	670	2,570
		61,340			61,340

Working Note : *D*'s share of goodwill ₹7,200 has been credited to his Current Account and debited to the Current Accounts of *R* and *L* in their gaining ratio of 2 : 1.

ILLUSTRATION 20.

M, N and *G* were partners in a firm sharing profits and losses in the ratio of 5 : 3 : 2. On 31-3-2016 their Balance Sheet was as under :

BALANCE SHEET OF *M, N* AND *G*

as at 31-3-2016

Liabilities		₹	*Assets*		₹
Creditors		55,000	Cash		40,000
General Reserve		30,000	Debtors	45,000	
Capitals :			*Less* : Provision	5,000	40,000
M	1,50,000		Stock		50,000
N	1,25,000		Machinery		1,50,000
G	75,000	3,50,000	Patents		30,000
			Building		1,00,000
			Profit & Loss A/c		25,000
		4,35,000			4,35,000

M retired on the above date and it was agreed that :

(i) Debtors of ₹2,000 will be written off as bad debts and a provision of 5% on debtors for bad and doubtful debts will be maintained.

(ii) Patents will be completely written off and stock, machinery and building will be depreciated by 5%.

(iii) An unrecorded creditor of ₹10,000 will be taken into account.

(iv) *N* and *G* will share the future profits in the ratio of 2 : 3.

(v) Goodwill of the firm on *M*'s retirement was valued at ₹3,00,000.

Pass necessary Journal Entries for the above transactions in the books of the firm on *M*'s retirement. *(C.B.S.E. 2017, Delhi)*

SOLUTION:

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2016 March 31	General Reserve A/c	Dr.		30,000	
	To *M*'s Capital A/c				15,000
	To *N*'s Capital A/c				9,000
	To *G*'s Capital A/c				6,000
	(General Reserve credited to all partners in 5 : 3 : 2)				
	M's Capital A/c	Dr.		12,500	
	N's Capital A/c	Dr.		7,500	
	G's Capital A/c	Dr.		5,000	
	To Profit & Loss A/c				25,000
	(Accumulated loss debited to all partners in 5 : 3 : 2)				
	N's Capital A/c (Note 1)	Dr.		30,000	
	G's Capital A/c	Dr.		1,20,000	
	To *M*'s Capital A/c				1,50,000
	(Adjustment for goodwill in the gaining ratio of 1 : 4)				
	Bad Debts A/c	Dr.		2,000	
	To Debtors A/c				2,000
	(Bad debts written off)				
	Provision for Bad Debts A/c	Dr.		2,850	
	To Bad Debts A/c				2,000
	To Revaluation A/c (Note 2)				850
	(Excess provision credited to revaluation account)				
	Revaluation A/c	Dr.		55,000	
	To Patents A/c				30,000
	To Stock A/c				2,500
	To Machinery A/c				7,500
	To Building A/c				5,000
	To Creditors A/c				10,000
	(Decrease in assets and increase in creditors)				

	M's Capital A/c	Dr.	27,075	
	N's Capital A/c	Dr.	16,245	
	G's Capital A/c	Dr.	10,830	
	To Revaluation A/c			54,150
	(Transfer of loss on revaluation)			
	M's Capital A/c	Dr.	2,75,425	
	To *M*'s Loan A/c (Note 4)			2,75,425
	(Balance due to *M* transferred to his Loan A/c)			

Working Notes :

(1) Gaining Ratio :

$$N : \frac{2}{5} - \frac{3}{10} = \frac{4-3}{10} = \frac{1}{10}$$

$$G : \frac{3}{5} - \frac{2}{10} = \frac{6-2}{10} = \frac{4}{10}$$

Gaining Ratio = 1 : 4

		₹
(2) Net Debtors : ₹45,000 – Bad Debts ₹2,000	=	43,000
Provision @ 5% on ₹43,000		2,150
Less : Existing Provision : ₹5,000 – Bad Debts ₹2,000	=	3,000
Excess Provision Credited to Revaluation Account		850

(3)

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Patents	30,000	By Provision for Bad Debts		850
To Stock	2,500	By Loss transferred to :		
To Machinery	7,500	*M*'s Capital A/c	27,075	
To Building	5,000	*N*'s Capital A/c	16,245	
To Creditors	10,000	*G*'s Capital A/c	10,830	54,150
	55,000			55,000

(4)

Dr. *M*'S CAPITAL ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Profit & Loss A/c	12,500	By Balance b/d	1,50,000
To Revaluation A/c (Loss)	27,075	By General Reserve A/c	15,000
To *M*'s Loan A/c	2,75,425	By *N*'s Capital A/c (Goodwill)	30,000
		By *G*'s Capital A/c (Goodwill)	1,20,000
	3,15,000		3,15,000

ILLUSTRATION 21.

Following is the Balance Sheet of *A*, *B* and *C* as at 31st March, 2022. They shared profits in the ratio of 2 : 2 : 1.

Liabilities		₹	*Assets*		₹
Sundry Creditors		5,00,000	Cash at Bank		10,000
General Reserve		2,50,000	Debtors	6,00,000	
Partners Loan A/cs :			*Less* : Provision for		
B	1,80,000		Doubtful Debts	25,000	5,75,000
C	1,20,000	3,00,000	Stock		3,40,000
Capital A/cs :			Land & Buildings		10,00,000
A	5,00,000		Advertisement Suspense A/c		60,000
B	3,00,000		Profit and Loss A/c		15,000
C	1,50,000	9,50,000			
		20,00,000			20,00,000

B retires on 1st April, 2022 on the following terms :

(*i*) Stock is overvalued by ₹20,000 and land & buildings are undervalued by ₹1,00,000.

(*ii*) Provision for doubtful debts is to be increased to ₹30,000.

(*iii*) Old credit balances of Sundry Creditors ₹40,000 be written off.

(*iv*) A computer purchased on 1st October, 2021 for ₹50,000 debited to Office Expenses Account is to be brought into account charging depreciation @ 20% p.a.

(*v*) Goodwill of the firm is valued at ₹1,50,000 and the amount due to *B* be adjusted in the capital accounts of *A* and *C*.

Prepare the Revaluation Account, Capital Accounts and the new Balance Sheet.

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Stock A/c		20,000	By Land & Buildings	1,00,000
To Provision for Doubtful Debts A/c		5,000	By Sundry Creditors A/c	40,000
To Profit on revaluation transferred to :			By Office Equipment (Computer)	45,000
A's Capital A/c	64,000			
B's Capital A/c	64,000			
C's Capital A/c	32,000	1,60,000		
		1,85,000		1,85,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Advertise-ment Sus-				By Bal. b/d	5,00,000	3,00,000	1,50,000
				By General			

pense A/c	24,000	24,000	12,000	Reserve	1,00,000	1,00,000	50,000
To Profit and Loss A/c	6,000	6,000	3,000	By Revaluation A/c	64,000	64,000	32,000
To B's Capital A/c (Goodwill)	40,000	—	20,000	By A's Capital A/c (Goodwill)	—	40,000	—
To B's Loan A/c	—	4,94,000	—	By C's Capital A/c (Goodwill)	—	20,000	—
To Balance c/d	5,94,000		1,97,000				
	6,64,000	5,24,000	2,32,000		6,64,000	5,24,000	2,32,000

BALANCE SHEET *as at 1st April, 2022*

Liabilities		₹	*Assets*		₹
Sundry Creditors		4,60,000	Cash at Bank		10,000
B's Loan A/c			Debtors	6,00,000	
(4,94,000 + 1,80,000)		6,74,000	*Less* : Provision for		
C's Loan A/c		1,20,000	Doubtful Debts	30,000	5,70,000
Capital Accounts :			Stock		3,20,000
A	5,94,000		Office Equipment (Computer)		45,000
C	1,97,000	7,91,000	Land and Buildings		11,00,000
		20,45,000			20,45,000

Working Notes :

(1) Computer purchased for ₹50,000 was wrongly debited to Office Expenses Account, whereas it should have been debited to Office Equipment Account. Depreciation for 6 months *i.e.* from 1st October 2017 to 31st March 2018 @ 20% p.a. has not been charged. Hence ₹45,000 (*i.e.* ₹50,000 – Dep. ₹5,000) will be adjusted by passing the following entry :

Office Equipment A/c	Dr.	45,000	
To Revaluation A/c			45,000

(2) *B*'s share of Goodwill = ₹1,50,000 × $\frac{2}{5}$ = ₹60,000. It will be adjusted by passing the following entry :

A's Capital A/c (60,000 × $\frac{2}{3}$)	Dr.	40,000	
C's Capital A/c (60,000 × $\frac{1}{3}$)	Dr.	20,000	
To *B*'s Capital A/c			60,000

ILLUSTRATION 22.

Prem, Kumar and Aarti were partners sharing profits in the ratio of 5 : 3 : 2. Their Balance Sheet as at 31st March, 2019 was as under :

BALANCE SHEET OF PREM, KUMAR AND AARTI
as at 31st March, 2019

Liabilities	₹	*Assets*	₹
Capitals :		Building	25,000

Prem	30,000		Plant and Machinery	15,000
Kumar	20,000		Investments	10,000
Aarti	20,000	70,000	Debtors	10,000
General Reserve		8,000	Stock	5,000
Investment Fluctuation Reserve		2,000	Cash	25,000
Sundry Creditors		10,000		
		90,000		90,000

On the above date, Kumar retired. The terms of retirement were :

(*i*) Kumar sold his share of goodwill to Prem for ₹8,000 and to Aarti for ₹4,000.

(*ii*) Stock was found to be undervalued by ₹1,000 and building by ₹7,000.

(*iii*) Investments were sold for ₹11,000.

(*iv*) There was an unrecorded creditor of ₹7,000.

(*v*) An amount of ₹30,000 was paid to Kumar in cash which was contributed by Prem and Aarti in the ratio of 2 : 1. The balance amount of Kumar was settled by accepting a Bill of Exchange in favour of Kumar.

Prepare the Revaluation Account, Capital Accounts of partners and the Balance Sheet of the reconstituted firm. *(C.B.S.E. 2020, Mumbai, Chennai)*

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars		*Amount*	*Particulars*	*Amount*
		₹		₹
To Sundry Creditors A/c		7,000	By Stock A/c	1,000
To Gain on Revaluation			By Building A/c	7,000
transferred to :			By Investments A/c (Profit on	
Prem's Capital A/c	1,000		Sale of Investments)	1,000
Kumar's Capital A/c	600			
Aarti's Capital A/c	400	2,000		
		9,000		9,000

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*Prem*	*Kumar*	*Aarti*	*Particulars*	*Prem*	*Kumar*	*Aarti*
	₹	₹	₹		₹	₹	₹
To Kumar's				By Balance b/d	30,000	20,000	20,000
Capital A/c	8,000	—	4,000	By General Reserve	4,000	2,400	1,600
To Cash A/c	—	30,000	—	By Investment			
To Bills				Fluctuation			
Payable A/c	—	5,600	—	Reserve	1,000	600	400
To Balance c/d	48,000	—	28,400	By Revaluation A/c	1,000	600	400
				By Prem's Capital			

				A/c (Goodwill)	—	8,000	—
				By Aarti's Capital A/c (Goodwill)	—	4,000	—
				By Cash A/c	20,000	—	10,000
	56,000	35,600	32,400		56,000	35,600	32,400

BALANCE SHEET OF PREM AND AARTI
as at 31st March, 2019

Liabilities		*Amount*	*Assets*	*Amount*
		₹		₹
Sundry Creditors		17,000	Cash	36,000
Bills Payable		5,600	Stock	6,000
Capitals :			Debtors	10,000
Prem	48,000		Plant & Machinery	15,000
Aarti	28,400	76,400	Building	32,000
		99,000		99,000

Working Notes :

(1) Entry for sale of Investments :

Bank A/c	Dr.	11,000	
To Investments			11,000

(2) Entry for transfer of profit on Investments :

Investments A/c	Dr.	1,000	
To Revaluation A/c			1,000

ILLUSTRATION 23.

Parth, Angad and Leesha are partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1 respectively. Angad retires and his claim, including Capital and entitlements from the firm including his share of Goodwill of the firm, is ₹50,000.

After this amount was determined, it was found that there was an unrecorded piece of furniture valued at ₹12,000 which had to be recorded.

Upon recording this piece of furniture, the revised amount due to Angad was determined and settled by giving him this piece of furniture and the balance in cash.

You are required to give the journal entries for recording the payment to Angad in the books of the firm.

(I.S.C. 2018)

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Furniture A/c	Dr.		12,000	
	To Revaluation A/c				12,000
	(Unrecorded asset recorded)				

Revaluation A/c Dr.		12,000	
To Parth's Capital A/c			6,000
To Angad's Capital A/c			4,000
To Leesha's Capital A/c			2,000
(Transfer of profit on revaluation)			
Angad's Capital A/c Dr.		54,000	
To Furniture A/c			12,000
To Bank A/c			42,000
(Angad's claim discharged)			

ILLUSTRATION 24.

The Balance Sheet of *X*, *Y* and *Z* who shared profits in the ratio of 2 : 2 : 1, was as follows as at 31st March, 2022 :

Liabilities		₹	*Assets*	₹
Sundry Creditors		70,000	Cash at Bank	20,000
Reserve		1,00,000	Sundry Assets	14,15,000
Capital Accounts :				
X	5,00,000			
Y	3,00,000			
Z	2,40,000	10,40,000		
Profit for the year 2021-22		2,25,000		
		14,35,000		14,35,000

The above balance sheet is incorrect, since *Y* has retired with effect from 1st December, 2021. No adjustments have been made consequent to *Y*'s retirement.

You are required to make them and redraft the Balance Sheet. The Goodwill of the firm was valued at ₹75,000.

SOLUTION :

CAPITAL ACCOUNTS

Dr. Cr.

Particulars	*X*	*Y*	*Z*	*Particulars*	*X*	*Y*	*Z*
31.3.2022	₹	₹	₹	31.3.2022	₹	₹	₹
To *Y*'s Capital A/c				By Balance b/d	5,00,000	3,00,000	2,40,000
(Goodwill)	20,000		10,000	By Reserve A/c	40,000	40,000	20,000
To Balance c/d	5,80,000	4,30,000	2,80,000	By *X*'s Capital A/c (Goodwill)		20,000	
				By *Z*'s Capital A/c (Goodwill)		10,000	
				By P & L Appropriation A/c (Share of			

				profit for 8 months)	60,000	60,000	30,000
	6,00,000	4,30,000	2,90,000		6,00,000	4,30,000	2,90,000
To Y's Loan A/c		4,55,000		By Balance b/d	5,80,000	4,30,000	2,80,000
To Balance c/d	6,13,333		2,96,667	By P & L Appropriation A/c (Share of Profit for 4 months)	33,333	25,000	16,667
	6,13,333	4,55,000	2,96,667		6,13,333	4,55,000	2,96,667

BALANCE SHEET of *X* and *Z*

as at 1st April, 2022

Liabilities		₹	*Assets*	₹
Sundry Creditors		70,000	Cash at Bank	20,000
Y's Loan Account		4,55,000	Sundry Assets	14,15,000
Capital Accounts :				
X	6,13,333			
Z	2,96,667	9,10,000		
		14,35,000		14,35,000

Working Note :

Distribution of Profit : (Assuming profits have accrued evenly throughout the year)

(*i*) Profits for 8 months upto the date of Y's retirement : $2,25,000 \times \frac{8}{12} = ₹1,50,000$

This amount will be distributed in the ratio of 2 : 2 : 1, *i.e.*

X ₹60,000; *Y* ₹60,000 and *Z* ₹30,000

(*ii*) Profits for remaining 4 months : $2,25,000 \times \frac{4}{12} = ₹75,000$

Out of this amount, *Y* will be entitled (at his option) to either of the following :

First alternative : Interest at 6% p.a. on the amount due to him :

$$4,30,000 \times \frac{6}{100} \times \frac{4}{12} = ₹8,600$$

Second alternative : Profit which has been earned by the firm with the help of the amount due to him :

$$\frac{4,30,000}{5,80,000 + 4,30,000 + 2,80,000} \times ₹75,000 = ₹25,000$$

Of the two alternatives mentioned above, *Y* will opt for second alternative since he will be entitled to ₹25,000 according to second alternative whereas he gets only ₹8,600 according to first.

The balance of ₹50,000 (*i.e.* 75,000 – 25,000 given to *Y*) will be distributed between *X* and *Z* in the ratio of 2 : 1 as under :

$X: 50{,}000 \times \frac{2}{3} = 33{,}333$

$Z: 50{,}000 \times \frac{1}{3} = 16{,}667$

Adjustment of Capitals according to the New Profit-sharing Ratio

ILLUSTRATION 25.

Leena, Madan and Naresh were partners in a firm sharing profits and losses in the ratio of 2 : 2 : 3. On 31st March, 2022, their Balance Sheet was as follows :

Liabilities			₹	*Assets*	₹
Trade Creditors			1,60,000	Land and Building	10,00,000
Bank Overdraft			44,000	Machinery	5,00,000
Long-term Debts			4,00,000	Furniture	7,00,000
Employees' Provident Fund			76,000	Investments	2,00,000
Capitals :	Leena	12,50,000		Closing Stock	8,00,000
	Madan	8,00,000		Sundry Debtors	4,00,000
	Naresh	10,50,000	31,00,000	Bank	80,000
				Deferred Advertisement Expenditure	1,00,000
			37,80,000		37,80,000

On 31st March, 2022, Madan retired from the firm and the remaining partners decided to carry on the business. It was decided to revalue assets and liabilities as under :

(*i*) Land and Building be appreciated by ₹2,40,000 and Machinery be depreciated by 10%.

(*ii*) 50% of Investments were taken over by the retiring partner at book value.

(*iii*) An old customer Mohit whose account was written off as bad debt has promised to pay ₹7,000 in settlement of his full debt of ₹10,000.

(*iv*) Provision for Doubtful Debts was to be made at 5% on debtors.

(*v*) Closing Stock will be valued at market price which is ₹1,00,000 less than the book value.

(*vi*) Goodwill of the firm be valued at ₹5,60,000 and Madan's share of goodwill be adjusted in the accounts of Leena and Naresh. Leena and Naresh decided to share future profits and losses in the ratio of 3 : 2.

(*vii*) The total capital of the new firm will be ₹32,00,000 which will be in the proportion of the profit-sharing ratio of Leena and Naresh.

(*viii*) Amount due to Madan was settled by accepting a Bill of Exchange in his favour payable after 4 months.

Prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet of the firm after Madan's retirement.

SOLUTION :

REVALUATION ACCOUNT

Dr. Particulars	₹	Particulars	Cr. ₹
To Machinery A/c	50,000	By Land and Building A/c	2,40,000
To Closing Stock A/c	1,00,000	By Sundry Debtors A/c[(1)]	7,000
To Provision for Doubtful Debts A/c (5% on ₹4,07,000)	20,350		
To Profit on Revaluation transferred to :			
Leena's Capital A/c 21,900			
Madan's Capital A/c 21,900			
Naresh's Capital A/c 32,850	76,650		
	2,47,000		2,47,000

PARTNERS' CAPITAL ACCOUNTS

Dr. Particulars	Leena ₹	Madan ₹	Naresh ₹	Particulars	Leena ₹	Madan ₹	Cr. Naresh ₹
To Deferred Advertisement Expenditure A/c	28,571	28,571	42,858	By Balance b/d	12,50,000	8,00,000	10,50,000
To Madan's Capital A/c[(2)]	1,60,000	—	—	By Revaluation A/c (Profit)	21,900	21,900	32,850
To Naresh's Capital A/c[(2)]	16,000	—	—	By Leena's Capital A/c[(2)]		1,60,000	16,000
To Investments A/c	—	1,00,000	—				
To Bills Payable A/c	—	8,53,329	—				
To Bal. c/d	10,67,329		10,55,992				
	12,71,900	9,81,900	10,98,850		12,71,900	9,81,900	10,98,850
To Bal. c/d[(3)]	19,20,000		12,80,000	By Balance b/d	10,67,329		10,55,992
				By Bank A/c (Bal. Fig.)	8,52,671		2,24,008
	19,20,000		12,80,000		19,20,000		12,80,000

BALANCE SHEET

as at 1st April, 2022

Liabilities	₹	Assets	₹
Trade Creditors	1,60,000	Land and Building	12,40,000
Bank Overdraft	44,000	Machinery	4,50,000
Bills Payable	8,53,329	Furniture	7,00,000

Long-term Debts		4,00,000	Closing Stock		7,00,000
Employees Provident Fund		76,000	Investments		1,00,000
Capitals : Leena	19,20,000		Sundry Debtors	4,07,000	
Naresh	12,80,000	32,00,000	*Less* : Provision for Doubtful Debts	20,350	3,86,650
			Bank (Working Note 4)		11,56,679
		47,33,329			47,33,329

Working Notes :

(1) Mohit, who has promised to pay ₹7,000 will treated as a Debtor just like other debtors of the business because most of the business transactions are conducted on the basis of faith. The same treatment has been provided by CBSE in its marking scheme.

(2) Calculation of Gaining Ratio :

Gaining Ratio = New Share – Old Share

Leena's Gain $= \frac{3}{5} - \frac{2}{7} = \frac{21-10}{35} = \frac{11}{35}$ (Gain)

Naresh's Gain $= \frac{2}{5} - \frac{3}{7} = \frac{14-15}{35} = \frac{1}{35}$ (Sacrifice)

As Leena is the only gaining partner, she will compensate not only the retiring partner (Madan) but also the sacrificing partner (Naresh).

Entry for Goodwill :

Leena's Capital A/c $(5,60,000 \times \frac{11}{35})$	Dr.	1,76,000	
To Madan's Capital A/c $(5,60,000 \times \frac{2}{7}$ or $\frac{10}{35})$			1,60,000
To Naresh's Capital A/c $(5,60,000 \times \frac{1}{35})$			16,000

(3) Capitals of the Partners in the New Firm :

Leena's Capital $(32,00,000 \times \frac{3}{5})$ = ₹19,20,000

Naresh's Capital $(32,00,000 \times \frac{2}{5})$ = ₹12,80,000

(4)

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	80,000	To Balance c/d	11,56,679
To Leena's Capital A/c	8,52,671		
To Naresh's Capital A/c	2,24,008		
	11,56,679		11,56,679

ILLUSTRATION 26.

On 31st March, 2022, the Balance Sheet of M/s. *P*, *Q* and *R* sharing profits and losses in the ratio of 2 : 3 : 2, stood as follows :

Liabilities		₹	*Assets*	₹
Capital Accounts :			Land & Buildings	1,00,000
P	1,00,000		Machinery	1,70,000
Q	1,50,000		Stock-in-Trade	50,000
R	1,00,000	3,50,000	Sundry Debtors	60,000
Sundry Creditors		50,000	Cash and Bank Balances	20,000
		4,00,000		4,00,000

On 31st March, 2022, *Q* desired to retire from the firm and the remaining partners decided to carry on. It was agreed to revalue the assets and liabilities on that date on the following basis :

(1) Land and buildings be appreciated by 30%.

(2) Machinery be depreciated by 20%.

(3) Stock to be valued at ₹45,000.

(4) Provision for bad debts be made at 5%.

(5) Old credit balances of Sundry Creditors ₹5,000 be written off.

(6) Goodwill of the entire firm be valued at ₹63,000 and *Q*'s share of the Goodwill be adjusted in the accounts of *P* and *R*, who share the future profits and losses in the ratio of 3 : 2.

(7) The total capital of the firm is to be the same as before retirement. Individual capital be in their profit sharing ratio.

(8) Amount due to *Q* is to be settled on the following basis : 50% on retirement and the balance 50% within one year.

Pass journal entries and prepare Capital Accounts of Partners, Cash Account and Balance Sheet as at 1.4.2022 of M/s *P* and *R*.

SOLUTION :

JOURNAL ENTRIES

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
31.3.22	Land & Buildings A/c	Dr.		30,000	
	Sundry Creditors A/c	Dr.		5,000	
	To Revaluation A/c				35,000
	(Increase in the value of assets and decrease in liabilities)				
	Revaluation A/c	Dr.		42,000	
	To Machinery A/c				34,000
	To Stock-in-Trade A/c				5,000
	To Provision for bad debts A/c				3,000
	(Decrease in the value of assets)				

P's Capital A/c Dr. *Q*'s Capital A/c Dr. *R*'s Capital A/c Dr. To Revaluation A/c (Loss on revaluation transferred to Capital Accounts)		2,000 3,000 2,000	 7,000
P's Capital A/c Dr. *R*'s Capital A/c Dr. To *Q*'s Capital A/c (*Q*'s share of goodwill adjusted to the accounts of continuing partners in their gaining ratio 11 : 4)[1]		19,800 7,200	 27,000
Bank A/c Dr. To *P*'s Capital A/c[2] To *R*'s Capital A/c[2] (Amount brought in by *P* and *R* to bring their capitals to profit sharing ratio)		1,61,000	 1,21,800 39,200
Q's Capital A/c Dr. To Bank A/c To *Q*'s Loan A/c (50% amount paid to *Q* and the balance transferred to his loan account)		1,89,000	 94,500 94,500

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	*P*	*Q*	*R*	*Particulars*	*P*	*Q*	*R*
	₹	₹	₹		₹	₹	₹
To Revaluation A/c	2,000	3,000	2,000	By Balance b/d	1,00,000	1,50,000	1,00,000
To *Q*'s Capital A/c (Goodwill)	19,800		7,200	By *P*'s Capital A/c (Goodwill)		19,800	
To Balance c/d	78,200	1,74,000	90,800	By *R*'s Capital A/c (Goodwill)		7,200	
	1,00,000	1,77,000	1,00,000		1,00,000	1,77,000	1,00,000
To Bank A/c		87,000		By Balance b/d	78,200	1,74,000	90,800
To *Q*'s Loan A/c		87,000		By Bank A/c (Balancing figure)	1,31,800		49,200
To Balance c/d	2,10,000		1,40,000				
	2,10,000	1,74,000	1,40,000		2,10,000	1,74,000	1,40,000

Dr. CASH AND BANK ACCOUNTS Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	20,000	By *Q*'s Capital A/c	87,000
To *P*'s Capital A/c	1,31,800	By Balance c/d	1,14,000
To *R*'s Capital A/c	49,200		
	2,01,000		2,01,000

BALANCE SHEET OF *P* and *R*
as at 1st April, 2022

Liabilities		₹	*Assets*		₹
Capital Accounts :			Land & Buildings		1,30,000
P	2,10,000		Machinery		1,36,000
R	1,40,000	3,50,000	Stock-in-Trade		45,000
Q's Loan		87,000	Sundry Debtors	60,000	
Sundry Creditors		45,000	*Less* : Provision	3,000	57,000
			Cash and Bank balances		1,14,000
		4,82,000			4,82,000

Working Notes :

(1) Calculation of Gaining Ratio on *Q*'s retirement :

Gaining Ratio = New Ratio – Old Ratio

P Gains $= \frac{3}{5} - \frac{2}{7} = \frac{21-10}{35} = \frac{11}{35}$

R Gains $= \frac{2}{5} - \frac{2}{7} = \frac{14-10}{35} = \frac{4}{35}$

Hence, Gaining Ratio between *P* and *R* = 11 : 4

(2) Adjustment of capitals according to new profit sharing ratio :
Total capital of the firm is to be the same as before retirement which is ₹3,50,000

		₹
Therefore,	*P*'s Capital in the new firm should be $\frac{3}{5}$th of 3,50,000	= 2,10,000
	P's Existing Capital	= 78,200
Hence,	*P* will bring in	= 1,31,800
	R's Capital in the new firm should be $\frac{2}{5}$th of 3,50,000	= 1,40,000
	R's Existing Capital	90,800
Hence,	*R* will bring in	49,200

Retirement and Settlement of Loan

It may be agreed among the partners that the principal amount will be paid in a few equal instalments. In such case interest will be credited to the Loan Account on the basis of the amount outstanding at the beginning of each year and the amount paid will be debited to the Loan Account.

While preparing Loan Account of a Partner, recording must be made for accrued interest on the loan. Accrued interest may be of two types :

(*i*) **Interest Accrued but not Due :** Interest accrued but not due means interest is recorded in the Loan A/c but it has not become due for payment. For example, if the interest is payable half-yearly in June and December and books of the firm are closed on 31st March 2022, interest will be credited to Loan A/c from January to March 2022 following the accrual concept. But, this interest for 3 months will become due for payment on 30th June 2022 alongwith the interest

from April to June 2022. Interest from January to March 2022 will be called 'Interest accrued but not due'.

(*ii*) **Interest Accrued and Due :** Interest accrued and due means interest recorded in the Loan A/c is due for payment. In the above example, interest for half year *i.e.*, from 1st January 2022 to 30th June 2022 will be called 'Interest accrued and due'.

It may be noted that both types of accrued interest mentioned above are recorded in the Partner's Loan A/c.

Example : *A*, *B* and *C* are partners in a firm. *C* retires on 1st January 2022 and amount due to *C* after all adjustments amounts to ₹1,00,000. It is agreed to pay this amount in half-yearly instalments of ₹50,000 each alongwith interest @ 12% p.a. If the books of the firm are closed on 31st March every year, *C*'s Loan A/c will appear as follows :

Dr. C's LOAN ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2022		₹	2022		₹
March 31	To Balance c/d	1,03,000	Jan. 1	By C's Capital A/c	1,00,000
			March 31	By Interest A/c (12% p.a. for 3 months)	3,000
		1,03,000			1,03,000
June 30	To Bank A/c (₹50,000 + ₹6,000)	56,000	April 1	By Balance b/d	1,03,000
"	To Balance c/d	50,000	June 30	By Interest A/c (12% p.a. on ₹1,00,000 for 3 months)	3,000
		1,06,000			1,06,000
Dec. 31	To Bank A/c (₹50,000 + ₹3,000)	53,000	July 1	By Balance b/d	50,000
			Dec. 31	By Interest A/c (12% p.a. on ₹50,000 for six months)	3,000
		53,000			53,000

In the above example, Interest of ₹3,000 from Jan. 1 to March 31, 2022 will be called 'Interest Accrued but not Due' and total interest of ₹6,000 from Jan. 1 to June 30, 2022 will be called 'Interest Accrued and Due'. Similarly, interest from July 1 to Dec. 31, 2022 ₹3,000 will also be called 'Interest Accrued and Due.'.

ILLUSTRATION 27.

Mohit and Keshav are two partners sharing profits and losses equally. The Balance Sheet of their firm as at 31st March, 2016, was as follows :

Liabilities	₹	*Assets*	₹
Creditors	12,330	Cash in Hand	13,000

General Reserve		2,000	Book Debts	10,200
Capital Accouunts :			Closing Stock	6,730
Mohit	19,030		Building	19,300
Keshav	18,870	37,900	Goodwill	3,000
		52,230		52,230

Keshav retires on 1st April, 2016 on which date :

(*i*) The Goodwill of the firm was valued at ₹9,000.

(*ii*) 20% of the General Reserve was kept aside as provision for doubtful debts.

(*iii*) There was a piece of furniture valued at ₹2,060 which was unrecorded in the books of the firm.

Mohit decided to pay off Keshav by giving him this piece of furniture and the balance in annual instalments of ₹8,000 along with interest @ 5% per annum.

You are required to prepare :

(*a*) Keshav's Capital Account.

(*b*) Keshav's Loan Account till it is finally closed.

(ISC Sample Paper, 2017)

SOLUTION :

Dr. KESHAV'S CAPITAL ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Goodwill A/c ($\frac{1}{2}$ of ₹3,000)	1,500	By Balance b/d	18,870
To Furniture A/c	2,060	By Mohit's Capital A/c (Goodwill)	4,500
To Keshav's Loan A/c — Transfer	21,640	By Revaluation A/c ($\frac{1}{2}$ of ₹2,060)	1,030
		By General Reserve A/c $\frac{1}{2}$ of (₹2,000 – ₹400)	800
	25,200		25,200

Dr. KESHAV'S LOAN ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2017			2016		
March 31	To Bank A/c (₹8,000 + ₹1,082)	9,082	April 1	By Keshav's Capital A/c	21,640
March 31	To Balance c/d	13,640	2017		
			March 31	By Interest A/c (₹21,640 × $\frac{5}{100}$)	1,082
		22,722			22,722

2018 March 31	To Bank A/c (₹8,000 + ₹682)	8,682	2017 April 1	By Balance b/d	13,640
March 31	To Balance c/d	5,640	2018 March 31	By Interest A/c (₹13,640 × $\frac{5}{100}$)	682
		14,322			14,322
2019 March 31	To Bank A/c	5,922	2018 April 1	By Balance b/d	5,640
			2019 March 31	By Interest A/c (₹5,640 × $\frac{5}{100}$)	282
		5,922			5,922

ILLUSTRATION 28.

Pihu, Geeta and Nita are partners in a firm, sharing profits and losses in the ratio of 3 : 2 : 1. On 31st March, 2015, their Balance Sheet was as under :

BALANCE SHEET OF PIHU, GEETA AND NITA

as at 31st March, 2015

Liabilities		₹	*Assets*		₹
Sundry Creditors		15,000	Cash at Bank		16,000
General Reserve		9,000	Sundry Debtors	25,000	
Capital A/cs			*Less* : Provision for		
Pihu	79,000		Doubtful Debts	(1,300)	23,700
Geeta	70,000		Stock		14,300
Nita	61,000	2,10,000	Plant and Machinery		60,000
			Land and Building		1,20,000
		2,34,000			2,34,000

Nita retires on 1st April, 2015, subject to the following adjustments :

(*a*) Land and Building to be reduced by 10%.

(*b*) Goodwill to be valued at ₹54,000.

(*c*) Provision for Doubtful Debts to be raised to 10% of the debtors, the excess provision being created from General Reserve. The balance of the General Reserve to be distributed amongst the partners.

(*d*) Creditors of ₹3,000 were paid by Pihu for which she is not to be reimbursed.

(*e*) The continuing partners to share profits and losses in future in the ratio of 5 : 4.

(*f*) Nita to be paid ₹29,800 on retirement and the remaining amount in two equal annual instalments together with interest @10% per annum on the outstanding balance. The first instalment of Nita's loan to be paid on 30th Sept., 2015.

You are required to prepare :

(*i*) Revaluation Account.

(*ii*) Partners' Capital Accounts.

(*iii*) Nita's Loan Account till it is finally closed. (*I.S.C. 2016*)

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Land and Building A/c	12,000	By Creditors		3,000
		By Loss on Revaluation transferred to :		
		Pihu's Capital A/c	4,500	
		Geeta's Capital A/c	3,000	
		Nita's Capital A/c	1,500	9,000
	12,000			12,000

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	*Pihu*	*Geeta*	*Nita*	*Particulars*	*Pihu*	*Geeta*	*Nita*
To Nita's Capital A/c	3,000	6,000		By Balance b/d	79,000	70,000	61,000
To Revaluation A/c	4,500	3,000	1,500	By General Reserve	3,900	2,600	1,300
To Bank A/c			29,800	By Pihu's Capital A/c (Goodwill)(1)			3,000
To Nita's Loan A/c			40,000	By Geeta's Capital A/c (Goodwill)(1)			6,000
To Balance c/d	75,400	63,600					
	82,900	72,600	71,300		82,900	72,600	71,300

Dr. NITA'S LOAN ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2016 March 31	To Bank A/c (₹20,000 + 4,000)	24,000	2015 April 1	By Nita's Capital A/c	40,000
March 31	To Balance c/d	20,000	2016 March 31	By Interest A/c	4,000
		44,000			44,000
2017 March 31	To Bank A/c	22,000	2016 April 1	By Balance b/d	20,000
			2017 March 31	By Interest A/c	2,000
		22,000			22,000

Working Note (1)

Gaining Ratio = New Ratio – Old Ratio

Pihu : $\frac{5}{9}-\frac{3}{6}=\frac{10-9}{18}=\frac{1}{18}$

Geeta : $\frac{4}{9}-\frac{2}{6}=\frac{8-6}{18}=\frac{2}{18}$

Gaining Ratio $=\frac{1}{18}:\frac{2}{18}$ or 1 : 2

ILLUSTRATION 29.

Khushboo, Leela and Meena were partners in a firm sharing profits in the ratio of 5 : 3 : 2. Their Balance Sheet on 31st March, 2015 was as follows :

BALANCE SHEET OF KHUSHBOO, LEELA AND MEENA
as at 31st March, 2015

Liabilities		₹	*Assets*	₹
Creditors		70,000	Bank	44,000
Capitals :			Debtors	24,000
Khushboo	90,000		Stock	60,000
Leela	56,000		Building	1,40,000
Meena	60,000	2,06,000	Profit and Loss A/c	8,000
		2,76,000		2,76,000

On April 1, 2015 Leela retired on the following terms :

(*i*) Building was to be depreciated by ₹10,000.

(*ii*) A Provision of 5% was to be made on debtors for doubtful debts.

(*iii*) Salary outstanding was ₹4,800.

(*iv*) Goodwill of the firm was valued at ₹1,40,000.

(*v*) Leela was to be paid ₹20,800 through cheque and the balance was to be paid in two equal quarterly instalments (starting from 30th June, 2015) along with interest @ 10% per annum.

Prepare Revaluation Account, Leela's Capital Account and her Loan Account till it is finally paid. (*C.B.S.E. Sample Paper, 2017*)

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Building A/c	10,000	By Loss transferred to :		
To Provision for Doubtful Debts A/c	1,200	Khushboo's Capital A/c	8,000	
To Salary Outstanding A/c	4,800	Leela's Capital A/c	4,800	
		Meena's Capital A/c	3,200	16,000
	16,000			16,000

Dr. LEELA'S CAPITAL ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Profit and Loss A/c	2,400	By Balance b/d	56,000
To Revaluation A/c (Loss)	4,800	By Khushboo's Capital A/c (Note 1)	30,000
To Bank A/c	20,800	By Meena's Capital A/c (Note 1)	12,000
To Leela's Loan A/c (Balancing figure)	70,000		
	98,000		98,000

Dr. LEELA'S LOAN ACCOUNT Cr.

Date	Particulars	₹	Date	Particulars	₹
2015			2015		
June 30	To Bank A/c (₹35,000 + ₹1,750)	36,750	April 1	By Leela's Capital A/c	70,000
Sept. 30	To Bank A/c (₹35,000 + ₹875)	35,875	June 30	By Interest A/c $(₹70,000 \times \frac{10}{100} \times \frac{3}{12})$	1,750
			Sept. 30	By Interest A/c $(₹35,000 \times \frac{10}{100} \times \frac{3}{12})$	875
		72,625			72,625

Note (1) : Leela's share in Goodwill = $₹1,40,000 \times \frac{3}{10} = ₹42,000$, which is contributed by Khushboo and Meena in their gaining ratio of 5 : 2.

ILLUSTRATION 30.

X, *Y* and *Z* were in partnership sharing profits in the ratio of 3 : 2 : 1. At 1st April, 2017 the Balance Sheet of the firm stood as follows :

Liabilities		₹	Assets	₹
Provision for Doubtful Debts		1,300	Cash at Bank	10,000
Sundry Creditors		15,000	Debtors	16,000
Capitals :			Stock	20,300
X	78,750		Machinery	60,000
Y	70,000		Land and Building	1,20,000
Z	61,250	2,10,000		
		2,26,300		2,26,300

Z retires on the above date and the new profit sharing ratio between *X* and *Y* will be 5 : 4. Following terms were agreed :

(1) Land and Buildings be reduced by 10%.

(2) Out of the insurance premium paid during the year ₹5,000 be carried forward as unexpired.

(3) There is no need of any provision for doubtful debts.

(4) Goodwill of the firm be valued at ₹54,000.

(5) *X* and *Y* decided that their capitals will be adjusted in their new profit sharing ratio, by bringing in or paying cash to the partners. *Z*'s A/c will be transferred to his Loan A/c.

(*a*) Pass necessary journal entries; prepare the capital accounts and the new balance sheet.

(*b*) *Z* is paid ₹9,300 on the date of retirement and the remaining amount in three equal instalments together with interest at the rate of 10% p.a. on the outstanding balance. Show *Z*'s Loan A/c for 3 years.

SOLUTION : (a) JOURNAL ENTRIES

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2017					
April 1	Prepaid Insurance A/c	Dr.		5,000	
	Provision for Doubtful Debts A/c	Dr.		1,300	
	To Revaluation A/c				6,300
	(Increase in the value of assets)				
	Revaluation A/c	Dr.		12,000	
	To Land and Buildings A/c				12,000
	(Decrease in the value of assets)				
	X's Capital A/c	Dr.		2,850	
	Y's Capital A/c	Dr.		1,900	
	Z's Capital A/c	Dr.		950	
	To Revaluation A/c				5,700
	(Loss on revaluation transferred)				
	X's Capital A/c	Dr.		3,000	
	Y's Capital A/c	Dr.		6,000	
	To *Z*'s Capital A/c				9,000
	(Goodwill adjusted in the gaining ratio 1 : 2)				
	Z's Capital A/c	Dr.		69,300	
	To Bank A/c				9,300
	To *Z*'s Loan A/c				60,000
	(Balance of *Z*'s Capital A/c transferred to his loan A/c)				
	Bank A/c(2)	Dr.		2,100	
	To *X*'s Capital A/c				2,100
	(Amount brought in by *X* to raise his capital to profit sharing ratio)				
	Y's Capital A/c(2)	Dr.		2,100	
	To Bank A/c				2,100
	(Amount withdrawn by *Y* to bring his capital to profit sharing ratio)				

CAPITAL ACCOUNTS

Dr. Cr.

Particulars	X	Y	Z	Particulars	X	Y	Z
	₹	₹	₹		₹	₹	₹
To Z's Capital A/c (Goodwill)	3,000	6,000	—	By Balance b/d	78,750	70,000	61,250
To Revaluation A/c	2,850	1,900	950	By X's Capital A/c (Goodwill)	—	—	3,000
To Bank A/c			9,300	By Y's Capital	—	—	6,000
To Z's Loan A/c			60,000				
To Balance c/d	72,900	62,100					
	78,750	70,000	70,250		78,750	70,000	70,250
To Bank A/c	—	2,100	—	By Balance b/d	72,900	62,100	—
To Balance c/d	75,000	60,000	—	By Bank A/c	2,100	—	—
	75,000	62,100	—		75,000	62,100	—

BALANCE SHEET

as at 1st April, 2017

Liabilities		₹	*Assets*	₹
Sundry Creditors		15,000	Cash at Bank (₹10,000 + ₹2,100 – ₹2,100 – ₹9,300)	700
Z's Loan		60,000	Debtors	16,000
Capitals :			Stock	20,300
X	75,000		Prepaid Insurance	5,000
Y	60,000	1,35,000	Machinery	60,000
			Land and Buildings	1,08,000
		2,10,000		2,10,000

Working Notes :

(1) Calculation of Gaining Ratio = New Ratio – Old Ratio

Gain to X $= \frac{5}{9} - \frac{3}{6} = \frac{1}{18}$

Gain to Y $= \frac{4}{9} - \frac{2}{6} = \frac{2}{18}$

Hence, Gaining Ratio $= \frac{1}{18} : \frac{2}{18} = 1 : 2$

(2) Adjustment of Capitals of X and Y according to new profit sharing ratio

= Total Capitals of X and Y after the adjustments of Revaluation and Goodwill

= ₹72,900 + ₹62,100 = ₹1,35,000

This Capital should be in their profit sharing ratio, *i.e.,* 5 : 4

Therefore, the Capital of X in the new firm should be $\frac{5}{9}$ th of 1,35,000 = ₹75,000

But the existing Capital of X is = ₹72,900

Hence, X will bring in = ₹ 2,100

The Capital of Y in the new firm should be $\frac{4}{9}$ th of 1,35,000 = ₹60,000

But the existing Capital of Y is = ₹62,100

Hence, Y will withdraw = ₹ 2,100

(b) Settlement of Loan Account :

Dr. Z's LOAN ACCOUNT Cr.

Date	Particulars	₹	Date	Particulars	₹
2018			2017		
March 31	To Bank A/c (₹20,000 + ₹6,000)	26,000	April 1	By Z's Capital A/c (transfer)	60,000
March 31	To Balance c/d	40,000	2018		
			March 31	By Interest A/c (on ₹60,000 at 10%)	6,000
		66,000			66,000
2019			2018		
March 31	To Bank A/c (₹20,000 + ₹4,000)	24,000	April 1	By Balance b/d	40,000
March 31	To Balance c/d	20,000	2019		
			March 31	By Interest A/c (on ₹40,000 at 10%)	4,000
		44,000			44,000
2020			2019		
March 31	To Bank A/c (₹20,000 + ₹2,000)	22,000	April 1	By Balance b/d	20,000
			2020		
			March 31	By Interest A/c (on ₹20,000 at 10%)	2,000
		22,000			22,000

ILLUSTRATION 31.

A, *B* and *C* are partners in a firm. *A* retires on 1st April, 2018. On the date of retirement, ₹80,000 is due to him in all. It is agreed to pay him this amount in instalments every year at the end of the year. Prepare *A*'s Loan A/c in the following cases :

(*i*) Four yearly instalments plus interest @ 10% p.a.

(*ii*) Three instalments of ₹25,000 which already include interest @ 10% p.a. on the outstanding balance and the balance including interest in the fourth year.

Books are closed on 31st March every year.

SOLUTION :

Case (i)

Dr. A's LOAN A/C Cr.

Date	Particulars	₹	Date	Particulars	₹
2019			2018		
March 31	To Bank (20,000 + 8,000)	28,000	April 1	By A's Capital A/c	80,000
			2019		
March 31	To Balance c/d	60,000	March 31	By Interest on ₹80,000 @ 10%	8,000
		88,000			88,000

2020			2019		
March 31	To Bank (20,000 + 6,000)	26,000	April 1	By Balance b/d	60,000
			2020		
March 31	To Balance c/d	40,000	March 31	By Interest on ₹60,000 @ 10%	6,000
		66,000			66,000
2021			2020		
March 31	To Bank (20,000 + 4,000)	24,000	April 1	By Balance b/d	40,000
			2021		
March 31	To Balance c/d	20,000	March 31	By Interest on ₹40,000 @ 10%	4,000
		44,000			44,000
2022			2021		
March 31	To Bank (20,000 + 2,000)	22,000	April 1	By Balance b/d	20,000
			2022		
			March 31	By Interest on ₹20,000 @ 10%	2,000
		22,000			22,000

Case (ii)

Dr. *A*'s LOAN A/C Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2019			2018		
March 31	To Bank	25,000	April 1	By *A*'s Capital A/c	80,000
March 31	To Balance c/d	63,000	2019		
			March 31	By Interest on ₹80,000 @ 10%	8,000
		88,000			88,000
2020			2019		
March 31	To Bank	25,000	April 1	By Balance b/d	63,000
March 31	To Balance c/d	44,300	2020		
			March 31	By Interest on ₹63,000 @ 10%	6,300
		69,300			69,300
2021			2020		
March 31	To Bank	25,000	April 1	By Balance b/d	44,300
March 31	To Balance c/d	23,730	2021		
			March 31	By Interest on ₹44,300 @ 10%	4,430
		48,730			48,730
2022			2021		
March 31	To Bank	26,103	April 1	By Balance b/d	23,730

			2022 March 31	By Interest on ₹23,730 @ 10%	2,373
		26,103			26,103

ILLUSTRATION 32.

Banwari, Girdhari and Murari are partners in a firm sharing profits and losses in the ratio of 4 : 5 : 6. On 31st March, 2014, Girdhari retired. On that date the capitals of Banwari, Girdhari and Murari before the necessary adjustments stood at ₹2,00,000, ₹1,00,000 and ₹50,000 respectively. On Girdhari's retirement, goodwill of the firm was valued at ₹1,14,000. Revaluation of assets and re-assessment of liabilities resulted in a profit of ₹6,000. General Reserve stood in the books of the firm at ₹30,000.

The amount payable to Girdhari was transferred to his loan account. Banwari and Murari agreed to pay Girdhari two yearly instalments of ₹75,000 each including interest @10% p.a. on the outstanding balance during the first two years and the balance including interest in the third year. The firm closes its books on 31st March every year.

Prepare Girdhari's loan account till it is finally paid showing the working notes clearly. *(C.B.S.E. 2018)*

SOLUTION :

Amount Due to Girdhari :	₹
Girdhari's Capital	1,00,000
Share of Goodwill : $1,14,000 \times \frac{5}{15}$	38,000
Share of Revaluation Profit : $6,000 \times \frac{5}{15}$	2,000
Share of General Reserve : $30,000 \times \frac{5}{15}$	10,000
	1,50,000

Dr. GIRDHARI'S LOAN A/C Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2014 March 31	To Balance c/d	1,50,000	2014 March 31	By Girdhari's Capital A/c	1,50,000
		1,50,000			1,50,000
2015 March 31	To Bank	75,000	2014 April 1	By Balance b/d	1,50,000
March 31	To Balance c/d	90,000	2015 March 31	By Interest on 1,50,000 @ 10%	15,000
		1,65,000			1,65,000

2016			2015		
March 31	To Bank	75,000	April 1	By Balance b/d	90,000
March 31	To Balance c/d	24,000	2016		
			March 31	By Interest on 90,000 @ 10%	9,000
		99,000			99,000
2017			2016		
March 31	To Bank	26,400	April 1	By Balance b/d	24,000
			2017		
			March 31	By Interest on 24,000 @ 10%	2,400
		26,400			26,400

ILLUSTRATION 33.

A, *B* and *C* were in partnership, sharing profits and losses in the ratio of 4 : 3 : 2. The balances on their Capital Accounts were :

	₹
A	2,25,000
B	1,50,000
C	1,20,000

On 31st March, 2015, *B* retired. The partners agreed to revalue certain assets as follows :

	Book value on 31st March, 2015	*Revised value*
	₹	₹
Machinery	27,450	22,950
Fixtures and Fittings	1,21,500	1,32,500
Debtors	1,80,000	1,60,000
Goodwill	—	90,000

B's current account at the date of retirement showed a debit balance of ₹7,425. Investments of the book value of ₹12,825 were transferred to *B* in part payment and ₹67,500 was settled in cash at the date of retirement.

According to the partnership agreement the amount outstanding on retirement was to be transferred to a loan account and repaid (at the end of each year) in three equal instalments plus interest at 8% per annum on the annual balance.

After *B*'s retirement, profits were to be shared in the ratio of 3 : 2 and all assets (except goodwill) would appear at their revised values.

Show the Partnership Accounts giving effect to these transactions.

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
31-3-2015		*31-3-2015*	

	₹			₹
To Machinery A/c	4,500	By Fixtures and Fittings A/c		11,000
To Provision for Doubtful Debts	20,000	By Loss on Revaluation :		
		A's Capital A/c (4/9)	6,000	
		B's Capital A/c (3/9)	4,500	
		C's Capital A/c (2/9)	3,000	13,500
	24,500			24,500

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
31-3-2015				*31-3-2015*			
To Revaluation A/c – loss	6,000	4,500	3,000	By Balance b/d	2,25,000	1,50,000	1,20,000
To *B*'s Capital A/c (Goodwill)	14,000		16,000	By *A*'s Capital A/c (Goodwill)		14,000	
To *B*'s Current A/c		7,425		By *C*'s Capital A/c (Goodwill)		16,000	
To Investments A/c		12,825					
To Cash A/c		67,500					
To *B*'s loan A/c		87,750					
To Balance c/d	2,05,000		1,01,000				
	2,25,000	1,80,000	1,20,000		2,25,000	1,80,000	1,20,000

Dr. *B*'S LOAN ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
31-3-2015		*31-3-2015*	
To Balance c/d	87,750	By *B*'s Capital A/c	87,750
31-3-2016		*1-4-2015*	
To Bank A/c (₹29,250 + ₹7,020)	36,270	By Balance b/d	87,750
To Balance c/d	58,500	31-3-2016	
		By Interest A/c (87,750 × 8%)	7,020
	94,770		94,770
31-3-2017		*1-4-2016*	
To Bank A/c (₹29,250 + ₹4,680)	33,930	By Balance b/d	58,500
To Balance c/d	29,250	31-3-2017	
		By Interest A/c (58,500 × 8%)	4,680
	63,180		63,180
31-3-2018		*1-4-2017*	
To Bank A/c (₹29,250 + ₹2,340)	31,590	By Balance b/d	29,250
		31-3-2018	
		By Interest A/c (29,250 × 8%)	2,340
	31,590		31,590

Working Note :

B's share of goodwill amounting to ₹30,000 (*i.e.* $\frac{3}{9}$ of ₹90,000) has been credited to B and debited to A and C in their gaining ratio calculated as below :

$$A = \frac{3}{5} - \frac{4}{9} = \frac{27-20}{45} = \frac{7}{45}$$

$$C = \frac{2}{5} - \frac{2}{9} = \frac{18-10}{45} = \frac{8}{45}$$

$$\text{Gaining Ratio} = 7:8$$

ILLUSTRATION 34.

P and Q were partners. On 31st March, 2019, P retired from active partnership and his share of the following was ascertained on the date of retirement :

	₹
Goodwill	1,00,000
Interest on Capital	2,500
Salary	7,500
Drawings	1,00,000
Interest on Drawings	10,000
Share of Profit	1,25,000
Capital	3,75,000

The amount due to P was to be kept with the firm as a loan bearing interest @ 10% p.a. and was to be paid to P by annual instalments of ₹2,50,000 each, interest being calculated @10% p.a. on the unpaid balances. The first instalment was paid on 31st March, 2020.

You are required to prepare P's Capital Account and also P's Loan Account until the payment of the whole amount due to him was made. Books are closed on 31st March every year.

SOLUTION :

Dr. P's CAPITAL ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Drawings A/c	1,00,000	By Balance b/d	3,75,000
To Interest on Drawings A/c	10,000	By Q' Capital A/c (Goodwill)	1,00,000
To P's Loan A/c — Transfer	5,00,000	By Interest on Capital A/c	2,500
		By Salary A/c	7,500
		By Profit and Loss Appropriation A/c (Share of Profit)	1,25,000
	6,10,000		6,10,000

Dr. P's LOAN ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2019 March 31	To Balance c/d	5,00,000	2019 March 31	By P's Capital A/c	5,00,000

2020			2019			
March 31	To Bank A/c	2,50,000	April 1	By Balance b/d		5,00,000
March 31	To Balance c/d	3,00,000	2020			
			March 31	By Interest A/c @ 10%		50,000
		5,50,000				5,50,000
2021			2020			
March 31	To Bank A/c	2,50,000	April 1	By Balance b/d		3,00,000
March 31	To Balance c/d	80,000	2021			
			March 31	By Interest A/c @ 10%		30,000
		3,30,000				3,30,000
2022			2021			
March 31	To Bank A/c	88,000	April 1	By Balance b/d		80,000
			2022			
			March 31	By Interest A/c @ 10%		8,000
		88,000				88,000

ILLUSTRATION 35.

Angad, Kunal and Nitin were partners sharing profit and losses in the proportion of 2 : 2 : 1 respectively. The Balance Sheet of their firm as at 31st March, 2013, stood as follows :

Liabilities		₹	*Assets*		₹
Capital Accounts :			Stock		12,500
Angad	12,500		Machinery		17,500
Kunal	15,000		Motor Van		4,000
Nitin	20,000	47,500	Buildings		22,500
Creditors		10,000	Bank		1,250
Bills Payable		2,000	Debtors	8,000	
General Reserve		6,000	*Less :* Provision for		
			Doubtful Debts	250	7,750
		65,500			65,500

Kunal retires on 1st April, 2013, subject to the following adjustments :

(*a*) Provision for bad and doubtful debts to be increased by ₹975

(*b*) Stock to be appreciated by 20% and Building by 10%.

(*c*) Machinery to be depreciated by 10% and Motor Van by 15%.

(*d*) Goodwill of the firm to be valued at ₹9,000.

(*e*) The capitals of the continuing partners are to be adjusted according to the new profit sharing ratio which is agreed between Angad and Nitin as 3 : 2 respectively.

(*f*) Excess or shortfall in Angad's and Nitin's Capital Accounts to be transferred to their respective Current Accounts.

You are required to prepare :

(*i*) Revaluation Account.

(*ii*) Partner's Capital Accounts.

(*iii*) Balance Sheet of the reconstituted firm. (I.S.C. 2014)

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Provision for Doubtful Debts A/c		975	By Stock A/c	2,500
To Machinery A/c		1,750	By Building A/c	2,250
To Motor Van A/c		600		
To Profit transferred to :				
Angad's Capital A/c	570			
Kunal's Capital A/c	570			
Nitin's Capital A/c	285	1,425		
		4,750		4,750

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*Angad*	*Kunal*	*Nitin*	*Particulars*	*Angad*	*Kunal*	*Nitin*
	₹	₹	₹		₹	₹	₹
To Kunal's Capital A/c (Goodwill)	1,800		1,800	By Balance b/d	12,500	15,000	20,000
To Kunal's Loan A/c		21,570		By General Reserve	2,400	2,400	1,200
To Balance c/d	13,670		19,685	By Revaluation A/c	570	570	285
				By Angad's Capital A/c (Goodwill)		1,800	
				By Nitin's Capital A/c (Goodwill)		1,800	
	15,470	21,570	21,485		15,470	21,570	21,485
To Nitin's Current A/c			6,343	By Balance b/d	13,670		19,685
To Balance c/d	20,013		13,342	By Angad's Current A/c	6,343		
	20,013		19,685		20,013		19,685

BALANCE SHEET (After Kunal's Retirement)

Liabilities		₹	*Assets*		₹
Creditors		10,000	Bank		1,250
Bills Payable		2,000	Debtors	8,000	
Kunal's Loan		21,570	*Less :* Provision for Doubtful Debts	1,225	6,775
Current A/c :					
Nitin		6,343	Stock		15,000
Capital A/cs :			Machinery		15,750
Angad	20,013		Motor Van		3,400

Nitin	13,342	33,355	Buildings Current A/c : Angad	24,750 6,343
		73,268		73,268

Working Notes :

(1) Kunal's share of Goodwill = ₹9,000 × $\frac{2}{5}$ = ₹3,600

It will be adjusted between Angad and Nitin in their gaining ratio :

Angad = $\frac{3}{5} - \frac{2}{5} = \frac{1}{5}$

Nitin = $\frac{2}{5} - \frac{1}{5} = \frac{1}{5}$ or 1 : 1

(2) New Ratio of Angad and Nitin = 3 : 2

Total Capital of the new firm after the retirement of Kunal :

	₹
Angad's existing Capital	13,670
Nitin's existing Capital	19,685
	33,355

Total Capital of the new firm should be divided between Angad and Nitin in their new profit sharing ratio *i.e.*, 3 : 2.

Angad's New Capital = 33,355 × $\frac{3}{5}$ = ₹20,013

Nitin's New Capital = 33,355 × $\frac{2}{5}$ = ₹13,342

Therefore, adjustment of Surplus/Deficit in their Current Accounts :

		Angad ₹		*Nitin* ₹
Capital Required		20,013		13,342
Less : Existing Capital		13,670		19,685
	Deficit	6,343	Surplus	6,343

Angad's Current A/c will be debited by ₹6,343

Nitin's Current A/c will be credited by ₹6,343

ILLUSTRATION 36.

W, X, Y and *Z* were partners in a firm sharing profits and losses in ratio of 4 : 3 : 2 : 1. The Balance Sheet of the firm as at 31st March, 2021 is given below :

BALANCE SHEET
as at 31st March, 2021

Liabilities	₹	*Assets*	₹
W's Capital	4,00,000	Land and Building	3,40,000
X's Capital	3,00,000	Plant and Machinery	4,50,000
Y's Capital	2,00,000	Furniture and Fittings	1,20,000
Z's Capital	1,00,000	Fixed Deposit with Bank	80,000
Reserves	50,000	Stock-in-Trade	35,000

Bills Payable	12,000	Sundry Debtors	26,000
Sundry Creditors	8,000	Bills Receivable	10,000
Bank Overdraft	5,000	Cash in Hand	14,000
	10,75,000		10,75,000

On 31st December, 2021, *W* retired from the firm. The Partnership Deed of the firm had following provisions regarding the procedure to be followed in the event of retirement of a partner :

(*i*) The retiring partner will be entitled to his share of profit in proportion to the number of months he served as a partner in the year of his retirement. The profit of the year immediately preceding the year of his retirement will be taken as the basis for calculating his share of profit.

(*ii*) The retiring partner will be entitled to his share of goodwill on the basis of two years' purchase of the average profit of three years preceding the year of his retirement. The profits for the years ending 31st March 2019, 2020 and 2021 were ₹66,000; ₹87,000 and ₹72,000 respectively.

(*iii*) Reserves, undistributed profit or loss, if any, must be transferred to the Capital Accounts of the Partners.

X, *Y* and *Z* decided to share future profits and losses equally and to maintain a fixed capital of ₹2,00,000 each, making necessary addition or withdrawal of cash immediately without affecting the bank overdraft balance. The total amount due to *W* will remain in the business of the firm as loan, earning 10% interest per annum.

Show the Journal entries and the Capital Accounts of the Partners on the basis of the above mentioned conditions, which were duly complied with.

SOLUTION :

Books of *W*, *X*, *Y* and *Z*

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2021					
Dec. 31	Reserves A/c	Dr.		50,000	
	To *W*'s Capital A/c				20,000
	To *X*'s Capital A/c				15,000
	To *Y*'s Capital A/c				10,000
	To *Z*'s Capital A/c				5,000
	(Reserves distributed among the partners)				
	X's Capital A/c	Dr.		1,800	
	Y's Capital A/c	Dr.		7,200	
	Z's Capital A/c	Dr.		12,600	
	To *W*'s Capital A/c				21,600
	(*W*'s share of estimated profit up to the date of his retirement credited to him and debited to *X*, *Y* and *Z* in the gaining ratio of 1 : 4 : 7)				

	X's Capital A/c ... Dr.		5,000	
	Y's Capital A/c ... Dr.		20,000	
	Z's Capital A/c ... Dr.		35,000	
	To W's Capital A/c			60,000
	(W's share of goodwill debited to the Capital Accounts of X, Y and Z in the gaining ratio of 1 : 4 : 7)			
	W's Capital A/c ... Dr.		5,01,600	
	To W's Loan A/c			5,01,600
	(Amount due to W transferred to his Loan Account)			
	Bank A/c ... Dr.		1,59,800	
	To Y's Capital A/c			17,200
	To Z's Capital A/c			1,42,600
	(Deficit of capital brought in by Y and Z)			
	X's Capital A/c ... Dr.		1,08,200	
	To Bank A/c			1,08,200
	(Surplus capital withdrawn by X)			

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	W	X	Y	Z	Particulars	W	X	Y	Z
	₹		₹	₹		₹	₹		₹
To W's Capital A/c	—	1,800	7,200	12,600	By Bal. b/d	4,00,000	3,00,000	2,00,000	1,00,000
To W's Capital A/c (Goodwill)	—	5,000	20,000	35,000	By Reserve	20,000	15,000	10,000	5,000
To W's Loan A/c—Transfer	5,01,600	—	—	—	By X's Capital A/c	1,800			
To Bank A/c	—	1,08,200	—	—	By Y's Capital A/c	7,200			
To Bal. c/d	—	2,00,000	2,00,000	2,00,000	By Z's Capital A/c	12,600			
					By X's Capital A/c (Goodwill)	5,000	—	—	—
					By Y's Capital A/c (Goodwill)	20,000	—	—	—
					By Z's Capital A/c				

					(Goodwill)	35,000	—	—	—
					By Bank A/c	—	—	17,200	1,42,600
	5,01,600	3,15,000	2,27,200	2,47,600		5,01,600	3,15,000	2,27,200	2,47,600

Working Notes :

(1) Calculation of Gaining Ratio = New Ratio – Old Ratio

$$X \text{ Gains} = \frac{1}{3} - \frac{3}{10} = \frac{10-9}{30} = \frac{1}{30}$$

$$Y \text{ Gains} = \frac{1}{3} - \frac{2}{10} = \frac{10-6}{30} = \frac{4}{30}$$

$$Z \text{ Gains} = \frac{1}{3} - \frac{1}{10} = \frac{10-3}{30} = \frac{7}{30}$$

Hence, Gaining Ratio of X, Y and Z = 1 : 4 : 7

(2) Calculation of W's share of goodwill :

$$\text{Average Profit} = \frac{₹66,000 + ₹87,000 + ₹72,000}{3} = ₹75,000$$

Value of Goodwill at 2 years' purchase = ₹75,000 × 2 = ₹1,50,000

W's Share of Goodwill = ₹1,50,000 × 4/10 = ₹60,000.

W's Share of Goodwill will be credited to W and debited to X, Y and Z in their Gaining Ratio of 1 : 4 : 7.

(3) W's share of profit upto the date of retirement =

$$₹72,000 \times \frac{9}{12} \times \frac{4}{10} = ₹21,600.$$

This amount will be credited to W and debited to X, Y and Z in their gaining ratio of 1 : 4 : 7. It should not be debited to Profit and Loss Suspense Account because the profit sharing ratio of continuing partners does not remain the same.

ILLUSTRATION 37.

A, *B* and *C* are partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. Their Balance Sheet as at 31-3-2022 is as follows :

BALANCE SHEET *as at 31-3-2022*

Liabilities		₹	*Assets*		₹
Capital Accounts :			Machinery at Cost	2,00,000	
A	1,20,000		*Less* : Provision for		
B	1,60,000		Depreciation	40,000	1,60,000
C	70,000	3,50,000	Furniture		10,000
Reserve		60,000	Motor Car		52,000
Sundry Creditors		90,000	Stock		1,84,000
			Sundry Debtors	80,000	
			Less : Provision	4,000	76,000

		Cash at Bank	18,000
	5,00,000		5,00,000

B retires on 30.6.2022 and *A* and *C* continue in partnership sharing profits in the ratio of 3 : 2. The terms of retirement provide the following :

(*i*) Machinery is to be valued at ₹1,85,000 and provision for doubtful debts would be ₹5,400.

(*ii*) Furniture was to be reduced to ₹6,000.

(*iii*) A provision of ₹2,600 is to be made for outstanding expenses.

(*iv*) Goodwill of the firm was to be valued at ₹27,000 and *B*'s share of the same was to be adjusted into the accounts of *A* and *C*. The profit upto the date of retirement was estimated at ₹36,000.

(*v*) *B* will take over the motor car at ₹50,000 and a bank loan of ₹1,50,000 is to be arranged for the balance amount payable to him on his retirement.

(*vi*) The capital of the new firm will be readjusted by bringing in or paying out cash so that the capital of *A* and *C* be in the new profit-sharing ratio.

Prepare journal entries, Capital Accounts of partners as at 30.6.2022 and a Balance Sheet as at that date.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
June 30	Reserve A/c	Dr.		60,000	
	To *A*'s Capital A/c				30,000
	To *B*'s Capital A/c				20,000
	To *C*'s Capital A/c				10,000
	(Reserve transferred to capital accounts)				
	Provision for Depreciation on Machinery A/c	Dr.		25,000	
	To Revaluation A/c				25,000
	(Increase in the value of assets)				
	Revaluation A/c	Dr.		10,000	
	To Provision for Doubtful Debts A/c				1,400
	To Furniture A/c				4,000
	To Outstanding Exp. A/c				2,600
	To Motor Car A/c				2,000
	(Decrease in the value of assets)				
	Revaluation A/c	Dr.		15,000	
	To *A*'s Capital A/c				7,500
	To *B*'s Capital A/c				5,000
	To *C*'s Capital A/c				2,500
	(Profit on revaluation transferred to capital accounts)				

	A's Capital A/c Dr. C's Capital A/c Dr. To B's Capital A/c (B's share of goodwill adjusted to the capital accounts of A and C in their gaining ratio i.e. 3 : 7)		2,700 6,300	9,000
	A's Capital A/c Dr. C's Capital A/c Dr. To B's Capital A/c (B's share of profit upto the date of retirement adjusted into the accounts of continuing partners in their gaining ratio 3 : 7) (Note 2)		3,600 8,400	12,000
	Bank A/c Dr. To Bank Loan A/c (Loan taken from bank)		1,50,000	1,50,000
	B's Capital A/c Dr. To Motor Car A/c To Bank A/c (Settlement of B's Account)		2,06,000	50,000 1,56,000
	A's Capital A/c Dr. To Bank A/c (Amount withdrawn by A to bring his capital to profit sharing ratio)		19,800	19,800
	Bank A/c Dr. To C's Capital A/c (Amount brought in by C to raise his capital to profit sharing ratio)		19,800	19,800

Dr. CAPITAL ACCOUNTS Cr.

Particulars	A	B	C	Particulars	A	B	C
30.6.2022	₹	₹	₹	*1-4-2022*	₹	₹	₹
To B's Capital A/c (Goodwill)	2,700		6,300	By Bal. b/d	1,20,000	1,60,000	70,000
				30.6.2022			
To B's Capital A/c (Profit)	3,600		8,400	By Reserve	30,000	20,000	10,000
				By Revaluation	7,500	5,000	2,500
To Motor Car A/c		50,000		By A's Capital A/c (Goodwill)		2,700	
To Bank A/c		1,56,000		By C's Capital A/c (Goodwill)		6,300	
To Bal. c/d	1,51,200		67,800	By A's Capital A/c (Profit)		3,600	
				By C's Capital A/c (Profit)		8,400	
	1,57,500	2,06,000	82,500		1,57,500	2,06,000	82,500
To Bank	19,800			By Bal. b/d	1,51,200		67,800

To Bal. c/d	1,31,400	87,600	By Bank		19,800
	1,51,200	87,600		1,51,200	87,600

BALANCE SHEET OF *A* AND *C*
as at 30-6-2022

Liabilities		₹	*Assets*		₹
Capital Accounts			Machinery at Cost	2,00,000	
A	1,31,400		*Less* : Provision for		
C	87,600	2,19,000	Depreciation	15,000	1,85,000
Bank Loan		1,50,000	Furniture		6,000
Sundry Creditors		90,000	Stock		1,84,000
Outstanding Expenses		2,600	Sundry Debtors	80,000	
			Less : Provision	5,400	74,600
			Cash at Bank		
			(18,000 + 1,50,000 – 1,56,000		
			+ 19,800 – 19,800)		12,000
		4,61,600			4,61,600

Working Notes :

(1) Calculation of gaining ratio on *B*'s retirement :

Gaining Ratio = New Ratio – Old Ratio

A Gains $= \frac{3}{5} - \frac{3}{6} = \frac{18-15}{30} = \frac{3}{30}$

C Gains $= \frac{2}{5} - \frac{1}{6} = \frac{12-5}{30} = \frac{7}{30}$

Hence, Gaining Ratio between *A* and *C* = 3 : 7

(2) *B*'s share of profit upto the date of retirement : ₹36,000 $\times \frac{2}{6}$ = ₹12,000.

This amount will be credited to *B* and debited to *A* and *C* in their gaining ratio of 3 : 7. It should not be debited to Profit and Loss Suspense Account because the profit sharing ratio of continuing partners, in between them, does not remain the same.

(3) Adjustments of Capitals of *A* and *C* according to new profit sharing ratio : ₹

Total Capitals of *A* and *C* after all adjustments

= ₹1,51,200 + ₹67,800 = 2,19,000

Hence, the Capital of *A* in the new firm should be $\frac{3}{5}$th of 2,19,000	=	1,31,400
But the existing Capital of *A* is		1,51,200
Hence, *A* will withdraw		19,800
The Capital of *C* in the new firm should be $\frac{2}{5}$th of 2,19,000	=	87,600
But the existing Capital of *C* is	=	67,800
Hence, *C* will bring in		19,800

ILLUSTRATION 38.

A, *B* and *C* were partners in a firm whose Balance Sheet as at 31st March, 2022 was as below :

Liabilities		₹	*Assets*	₹
Creditors		7,096	Cash at Bank	6,496
General Reserve		3,000	Debtors	9,000
Capitals :			Stock	10,600
A	8,000		Furniture	2,000
B	6,000			
C	4,000	18,000		
		28,096		28,096

B retired on 1st April, 2022 and in this connection it was decided to make the following adjustments :

(*a*) To reduce stock and furniture by 5% and 10% respectively; and

(*b*) To provide for doubtful debts at 5% on debtors.

Rent outstanding (not provided for as yet) was ₹260. Goodwill was valued at ₹4,200. *A* and *C* decided :

(*i*) To share profits and losses in 5 : 3 respectively;

(*ii*) To readjust their capitals in the profit sharing ratio; and

(*iii*) To bring in sufficient cash to pay off *B* immediately and to leave a balance of ₹1,000 in the Bank. *B* was paid off.

Give Journal entries to record the above and draft the Balance Sheet of the new firm.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2022					
April 1	General Reserve A/c	Dr.		3,000	
	To *A*'s Capital A/c				1,000
	To *B*'s Capital A/c				1,000
	To *C*'s Capital A/c				1,000
	(General reserve transferred to capital accounts)				
	Revaluation A/c	Dr.		1,440	
	To Stock A/c				530
	To Furniture A/c				200
	To Provision for Bad Debts A/c				450
	To Outstanding Rent A/c				260
	(Decrease in the value of assets and provision made for outstanding rent)				
	A's Capital A/c	Dr.		480	
	B's Capital A/c	Dr.		480	
	C's Capital A/c	Dr.		480	
	To Revaluation A/c				1,440
	(Loss on Revaluation transferred to Capital Accounts)				

A's Capital A/c	Dr.		1,225	
C's Capital A/c	Dr.		175	
To *B*'s Capital A/c				1,400
(*B*'s share of goodwill adjusted to the accounts of *A* and *C* in their gaining ratio 7 : 1)				
Bank A/c(2)	Dr.		2,424	
To *A*'s Capital A/c				1,495
To *C*'s Capital A/c				929
(Cash brought in, to make their capitals in profit sharing ratio)				
B's Capital A/c	Dr.		7,920	
To Bank A/c				7,920
(Amount due to *B* paid off)				

CAPITAL ACCOUNTS

Dr. Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Revaluation	480	480	480	By Balance b/d	8,000	6,000	4,000
To *B*'s Capital A/c	1,225	—	175	By Gen. Reserve	1,000	1,000	1,000
To Balance c/d	7,295	7,920	4,345	By *A*'s Capital A/c	—	1,225	—
				By *C*'s Capital A/c	—	175	—
	9,000	8,400	5,000		9,000	8,400	5,000
To Bank	—	7,920	—	By Balance b/d	7,295	7,920	4,345
To Balance c/d	8,790	—	5,274	By Bank	1,495	—	929
	8,790	7,920	5,274		8,790	7,920	5,274

BALANCE SHEET OF THE NEW FIRM

as at 1st April, 2022

Liabilities		₹	*Assets*		₹
Creditors		7,096	Cash at Bank		1,000
Outstanding Rent		260	Debtors	9,000	
			Less : Provision	450	8,550
Capitals :			Stock		10,070
A	8,790		Furniture		1,800
C	5,274	14,064			
		21,420			21,420

Total Capital of the new firm after *B*'s retirement should be :	₹
Amount required to pay off *B*	7,920
Add : Existing Capital of *A*	7,295
Add : Existing Capital of *C*	4,345
Add : Cash required as working capital	1,000
	20,560
Less : Cash at Bank (existing in Balance Sheet)	6,496
Total Capital of the new firm	14,064

This Capital should be in the new profit sharing ratio of A and C :

Therefore, A's new Capital should be $= 14{,}064 \times \frac{5}{8} = 8{,}790$

C's new Capital should be $= 14{,}064 \times \frac{3}{8} = 5{,}274$

Amount to be brought in by A and C :		
Capital required in the new firm	8,790	5,274
Less : Existing Capital	7,295	4,345
	1,495	929

Hidden Goodwill :

Sometimes the firm agrees to settle the retiring or deceased partner's account by payment of a lump sum amount. If such amount is in excess of his capital and share in reserves / revaluation etc. the excess will be treated as his share of goodwill.

For example, if retiring partner's Capital after all adjustments is ₹4,50,000 and if he is agreed to be paid ₹5,00,000; the excess paid, *i.e.*, ₹50,000 will be his share of goodwill. This will be recorded by debiting continuing partner's Capital accounts in gaining ratio and crediting retiring partner's capital account. It can be explained with the help of the following illustration :

ILLUSTRATION 39.

A, B and C are partners sharing profits in the ratio of 1 : 2 : 3. C retires and his capital, after making adjustments for reserves and profit on revaluation stands at ₹1,20,000. A and B agreed to pay him ₹1,50,000 in full settlement of his claim. Record necessary journal entry for the treatment of goodwill if the new profit sharing ratio is decided at 1 : 3.

SOLUTION :

	₹
Amount agreed to be paid in full settlement	1,50,000
Less : C's Capital (after all adjustments)	1,20,000
C's share of Hidden Goodwill	30,000

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	A's Capital A/c	Dr.		5,000	
	B's Capital A/c	Dr.		25,000	
	To C's Capital A/c				30,000
	(C's share of goodwill adjusted to the capital accounts of A and B in their gaining ratio 1 : 5)				

Calculation of Gaining Ratio :

A Gains $= \frac{1}{4} - \frac{1}{6} = \frac{3-2}{12} = \frac{1}{12}$

B Gains $= \frac{3}{4} - \frac{2}{6} = \frac{9-4}{12} = \frac{5}{12}$

Death of a Partner

On the death of a partner, the amount payable to him is to be paid to his legal representatives.

Calculation of the total amount due to the representatives of the deceased partner :

On the death of a partner, accounts in the books of the firm are maintained in the same way as on the retirement of a partner. Thus the legal representatives of the deceased partner are entitled to claim the following amounts, which are credited to his capital account :

1. The amount standing to the credit of his Capital A/c.
2. His share of the increase in the value of Goodwill of the firm.
3. Interest on Capital, if provided in the partnership deed.
4. His share of profit on the revaluation of assets and liabilities.
5. His share of the undistributed profits or reserves.
6. His share of Life Policy.
7. His share of profit upto the date of his death.

The following amounts will be debited to the account of the deceased partner for ascertaining the amount due to his legal representatives :

1. Drawings
2. Interest on drawings
3. His share of loss on the revaluation of assets and liabilities.
4. His share of undistributed loss, such as debit balance of Profit and Loss Account.
5. His share of loss that may have incurred till the date of his death.
6. His share of reduction in the value of goodwill.

All of the above mentioned adjustments are first made in the deceased partner's capital account and then the balance of his capital account is transferred to his executor's account.

The legal representative of a deceased partner is entitled, at his discretion, to interest at 6% p.a. on the amount due from the date of death to the date of payment or to that portion of profit which is earned by the firm with the amount due to the deceased partner.

Calculation of Profit :— If the death of a partner occurs on any day during the year, the executors of the deceased partner will also be entitled to the share of profits earned by the firm from the beginning of the year till the date of his death. Such profit may be ascertained from any of the following methods :

(A) On Time Basis.

(B) On Turnover or Sales Basis.

(A) **On Time Basis :—** In this method, we have to take into consideration the profit of the last year and the time for which he remained a partner during the current year. On the basis of last year's profit we shall calculate the proportionate profit upto the date of death and then calculate the deceased partner's share :

ILLUSTRATION 40.

A, *B* and *C* are partners in a firm whose books are closed on March 31st each year. *A* died on 30th June 2022 and according to the agreement the share of profits of a deceased partner up to the date of the death is to be calculated on the basis of the average profits for the last five years. The net profits for the last 5 years have been : 2018 ₹14,000; 2019 ₹18,000; 2020 ₹16,000; 2021 ₹10,000 (loss) and 2022 ₹16,000. Calculate *A*'s share of the profits upto the date of death and pass necessary journal entry assuming :

(*a*) there is no change in the profit sharing ratio of remaining partners;

(*b*) there is change in the profit sharing ratio of remaining partners, new ratio being 3 : 2.

SOLUTION :

Total Profit = ₹14,000 + 18,000 + 16,000 – 10,000 + 16,000 = 54,000

Average Profit = ₹54,000 ÷ 5 = ₹10,800

3 Month's Profit *i.e.* from 1st April 2022 to 30th June 2022 = $10{,}800 \times \frac{3}{12}$

= ₹2,700

$\frac{1}{3}$ rd share of *A* upto the date of death = $2{,}700 \times \frac{1}{3}$ = ₹900

Case (*i*) When there is no change in the profit sharing ratio of *B* and *C* :

JOURNAL ENTRY

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2022					
June 30	Profit and Loss Suspense A/c	Dr.		900	
	To *A*'s Capital A/c				900
	(*A*'s share of profit till the date of his death)				

Case (*ii*) When there is change in the profit sharing ratio of *B* and *C* and their new ratio is 3 : 2.

Gaining Ratio = New Ratio – Old Ratio

B Gains $= \frac{3}{5} - \frac{1}{3} = \frac{9-5}{15} = \frac{4}{15}$

C Gains $= \frac{2}{5} - \frac{1}{3} = \frac{6-5}{15} = \frac{1}{15}$

Hence, Gaining Ratio of *B* and *C* = 4 : 1

JOURNAL ENTRY

Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
2022				₹	₹
June 30	*B*'s Capital A/c ($900 \times \frac{4}{5}$)	Dr.		720	
	C's Capital A/c ($900 \times \frac{1}{5}$)	Dr.		180	
	To *A*'s Capital A/c				900
	(*B*'s share of profit debited to remaining partners in their gaining ratio of 4 : 1)				

ILLUSTRATION 41.

A, *B* and *C* were partners in a firm sharing profits in 3 : 2 : 1 ratio. The firm closes its books on 31st March every year. *B* died on 12-6-2022. On *B*'s death the goodwill of the firm was valued at ₹60,000. On *B*'s death his share in the profits of the firm till the time of his death was to be calculated on the basis of previous year's profit which was ₹1,50,000. Calculate *B*'s share in the profit of the firm. Pass necessary journal entries for the treatment of goodwill and *B*'s share of profit at the time of his death.

SOLUTION :

Working Notes :

(*i*) *B*'s share of Goodwill = ₹60,000 $\times \frac{2}{6}$ = ₹20,000. It will be debited to the Capital accounts of *A* and *C* in their gaining ratio, *i.e.* 3 : 1.

(*ii*) Number of days from March 31 to June 12 = 73.

B's share of Profit = 1,50,000 $\times \frac{73}{365} \times \frac{2}{6}$ = ₹10,000

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022 June 12					
(*i*)	*A*'s Capital A/c	Dr.		15,000	
	C's Capital A/c	Dr.		5,000	
	To *B*'s Capital A/c				20,000
	(*B*'s share of goodwill adjusted into the Capital A/cs of *A* and *C* in their gaining ratio, *i.e.*, 3 : 1)				
(*ii*)	Profit and Loss Suspense A/c	Dr.		10,000	
	To *B*'s Capital A/c				10,000
	(*B*'s share of profit up to June 12, 2022)				

(B) **On Turnover or Sales Basis :—** In this method, we have to take into consideration the profit and the total sales of the last year. Thereafter, the profit of the current year is estimated on the basis of the sales for the last year and the sales upto the date of death.

ILLUSTRATION 42.

X, *Y* and *Z* were partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1. The firm closes its books on 31st March every year. *Y* died on 24th June, 2018. *Y*'s share in the profits of the firm till the date of death from the last Balance Sheet was to be calculated on the basis of sales. Sales during the year 2017-18 was ₹15,00,000 and profit earned during the year was ₹3,00,000. Sales from 1st April, 2018 to 24th June, 2018 were ₹2,00,000. On *Y*'s death goodwill of the firm was valued at ₹1,20,000. The total amount payable to *Y*'s executors on his death was ₹1,75,000. This amount was paid to them on 15-7-2018.

Pass the necessary journal entries for the above transactions in the books of the firm. *(C.B.S.E. 2020, Punjab)*

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2018 June 24	Profit and Loss Suspense A/c[(1)] To Y's Capital A/c (Y's share of profit till the date of death)	Dr.		16,000	16,000
,,	X's Capital A/c Z's Capital A/c To Y's Capital A/c (Y's share of goodwill adjusted into the Capital A/cs of X and Z in their gaining ratio of 2 : 1)	Dr. Dr.		32,000 16,000	48,000
,,	Y's Capital A/c To Y's Executor's A/c (Y's Capital A/c transferred to his Executor's A/c)	Dr.		1,75,000	1,75,000
July 15	Y's Executor's A/c To Bank A/c (Amount paid to Y's Executors)	Dr.		1,75,000	1,75,000

Working Notes :

(1) Calculation of Y's Share of Profit :

(*i*) Ratio of Profit to Sales $= \dfrac{\text{Profit (Last Year)}}{\text{Sales (Last Year)}} \times 100$

$= \dfrac{3,00,000}{15,00,000} \times 100 = 20\%$

(*ii*) Profit upto the date of death $= 2,00,000 \times \dfrac{20}{100} =$ ₹40,000

(*iii*) Y's Share of Profit $= 40,000 \times \dfrac{2}{5} =$ ₹16,000

ILLUSTRATION 43.

Danish, Ana and Pranjal are partners in a firm sharing profits and losses in the ratio of 5 : 3 : 2. Their books are closed on March 31st every year.

Danish died on September 30th, 2019. The executors of Danish are entitled to :

(*i*) His share of Capital *i.e.,* ₹5,00,000 along-with his share of goodwill. The total goodwill of the firm was valued at ₹60,000.

(*ii*) His share of profit up to his date of death on the basis of sales till date of death. Sales for the year ended March 31, 2019 was ₹2,00,000 and profit for the same year was 10% on sales. Sales shows a growth trend of 20% and percentage of profit earning is reduced by 1%.

(*iii*) Half the amount was paid to Danish's Executor's immediately.

Pass necessary Journal Entries and show the workings clearly.

(C.B.S.E. Sample Paper, 2019)

SOLUTION:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019 Sept. 30	Ana's Capital A/c	Dr.		18,000	
	Pranjal's Capital A/c	Dr.		12,000	
	To Danish's Capital A/c				30,000
	(Danish's share of goodwill adjusted in Capital Accounts of Ana and Pranjal)				
	Profit and Loss Suspense A/c	Dr.		5,400	
	To Danish's Capital A/c				5,400
	(Danish's Share of Profit up to date of his death transferred to his capital account)				
	Danish's Capital A/c	Dr.		5,35,400	
	To Danish's Executor's A/c				5,35,400
	(Amount due to Danish transferred to his executor's account)				
	Danish's Executor's A/c	Dr.		5,35,400	
	To Bank A/c				2,67,700
	To Danish's Executor's Loan A/c				2,67,700
	(Half amount paid to Executor's)				

Working Notes :

Sales = 2,00,000 + 20% of 2,00,000

= 2,00,000 + 40,000 = ₹2,40,000

Profit % = 10% – 1% = 9%

Profit for six months = $₹2,40,000 \times \frac{9}{100} \times \frac{6}{12} = ₹10,800$

Danish's Share of Profit = $₹10,800 \times \frac{5}{10} = ₹5,400$

ILLUSTRATION 44.

The Balance Sheet of Sudha, Rahim and Kartik who were sharing profit in the ratio of 3 : 3 : 4 as at 31st March, 2022 was as follows :

Liabilities		Amount	Assets	Amount
		₹		₹
General Reserve		10,000	Cash	16,000
Bills Payable		5,000	Stock	44,000
Loan		12,000	Investments	47,000
Capitals : Sudha	60,000		Land & Building	60,000
Rahim	50,000		Sudha's Loan	10,000
Kartik	40,000	1,50,000		
		1,77,000		1,77,000

Sudha died on June 30th 2022. The partnership deed provided for the following on the death of a partner :

(*a*) Goodwill of the firm be valued at two years purchase of average profits for the last three years.

(*b*) Sudha's share of profit or loss till the date of her death was to be calculated on the basis of sales. Sales for the year ended 31st March, 2022 amounted to ₹4,00,000 and that from 1st April to 30th June 2022 to ₹1,50,000. The profit for the year ended 31st March, 2022 was ₹1,00,000.

(*c*) Interest on capital was to be provided @ 6% p.a.

(*d*) The average profits of the last three years were ₹42,000.

Prepare Sudha's Capital Account to be rendered to her executor.

SOLUTION :

SUDHA'S CAPITAL ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Sudha's Loan A/c	10,000	By Balance b/d	60,000
To Sudha's Executor's A/c	90,350	By General Reserve	3,000
		By Rahim's Capital A/c (Share of Goodwill) (₹25,200 × 3/7)	10,800
		By Kartik's Capital A/c (Share of Goodwill) (₹25,200 × 4/7)	14,400
		By Interest on Capital	900
		By Profit & Loss Suspense A/c (Share of Profit) (Note 2)	11,250
	1,00,350		1,00,350

Working Notes :

1. **Calculation of Sudha's Share of Goodwill :**

Value of firm's Goodwill = Average Profits of last three years × two years Purchase.
= ₹42,000 × 2 = ₹84,000

Sudha's Share of Goodwill = ₹84,000 × 3/10 = ₹25,200

2. **Calculation of Sudha's Share of Profit :**

(*i*) Ratio of Profit to Sales $= \dfrac{\text{Profit (Last Year)}}{\text{Sales (Last Year)}} \times 100 = \dfrac{₹1,00,000}{₹4,00,000} \times 100 = 25\%$

(*ii*) Profit (from 1st April to 30th June, 2022)
= ₹1,50,000 × 25/100 = ₹37,500

(*iii*) Sudha's Share of Profit = ₹37,500 × 3/10 = ₹11,250.

ILLUSTRATION 45.

A, *B* and *C* were partners in a firm sharing profits in the ratio of 5 : 4 : 3. On 31st March, 2021 their Balance Sheet was as under :

Liabilities		₹	*Assets*	₹
Creditors		24,000	Buildings	20,000
Reserves		6,000	Machinery	30,000
A's Capital	30,000		Stock	10,000
B's Capital	25,000		Patents	11,000

C's Capital	15,000	70,000	Debtors	8,000
			Cash at Bank	9,000
			Advertisement Suspense	12,000
		1,00,000		1,00,000

A died on 1st October, 2021 and *B* and *C* decided to share future profits in the ratio of 7 : 5. It was agreed between his executors and the remaining partners that :

(*a*) Goodwill to be valued at $2\frac{1}{2}$ years purchase of the average profits of the previous four years, which were :
2018 : ₹19,000; 2019 : ₹15,000; 2020 : ₹20,000 and 2021 : ₹18,000.

(*b*) Patents be valued at ₹8,000; Machinery at ₹28,000; and Buildings at ₹25,000.

(*c*) Profit for the year 2021-22 be taken as having accrued at the same rate as that of the previous year.

(*d*) Interest on Capital be provided at 10% p.a.

(*e*) Half of the amount due to *A* to be paid immediately to the executor and the balance transferred to his (Executor) Loan A/c.

Prepare *A*'s Capital A/c and *A*'s Executor's A/c as on 1st October, 2021.

SOLUTION :

(*i*) Calculation of Gaining Ratio :

$$B \text{ Gains} = \frac{7}{12} - \frac{4}{12} = \frac{3}{12}$$

$$C \text{ Gains} = \frac{5}{12} - \frac{3}{12} = \frac{2}{12}$$

Thus Gaining Ratio = 3 : 2.

(*ii*) Valuation of Goodwill :

Total Profit = 19,000 + 15,000 + 20,000 + 18,000 = ₹72,000

$$\text{Average Profit} = \frac{72{,}000}{4} = ₹18{,}000$$

Hence, Goodwill at $2\frac{1}{2}$ years purchase = $18{,}000 \times 2\frac{1}{2} = 45{,}000$

A's share of Goodwill = $45{,}000 \times \frac{5}{12} = 18{,}750$

It will be adjusted into the Capital Accounts of *B* and *C* in the gaining ratio of 3 : 2

(*iii*) Share of profit payable to *A* (upto the date of death) :

$$18{,}000 \times \frac{6}{12} \times \frac{5}{12} = ₹3{,}750$$

This amount of ₹3,750 will be credited to *A* and debited to *B* and *C* in their gaining ratio of 3 : 2.

Note : This amount of ₹3,750 should not be debited to Profit & Loss Suspense A/c because the profit sharing ratio of *B* and *C*, in between them, does not remain the same. Profit Sharing Ratio between *B* and *C* has changed from 4 : 3 to 7 : 5.

(*iv*)

REVALUATION ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Patents A/c	3,000	By Buildings A/c	5,000
To Machinery A/c	2,000		
	5,000		5,000

There is neither profit nor loss due to revaluation of assets.

A's CAPITAL ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Advertisement Suspense A/c		By Balance b/d	30,000
$(12{,}000 \times \frac{5}{12})$	5,000	By Reserves $(6{,}000 \times \frac{5}{12})$	2,500
To *A*'s Executor's A/c	51,500	By *B*'s Capital A/c (Goodwill)	
		$(18{,}750 \times \frac{3}{5})$	11,250
		By *C*'s Capital A/c (Goodwill)	
		$(18{,}750 \times \frac{2}{5})$	7,500
		By *B*'s Capital A/c (Share of Profit)	
		$(3{,}750 \times \frac{3}{5})$	2,250
		By *C*'s Capital A/c (Share of Profit)	
		$(3{,}750 \times \frac{2}{5})$	1,500
		By Interest on Capital	
		$(30{,}000 \times \frac{10}{100} \times \frac{6}{12})$	1,500
	56,500		56,500

A's EXECUTOR'S ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Bank A/c	25,750	By *A*'s Capital A/c	51,500
To *A*'s Executor's Loan A/c			
— Transfer	25,750		
	51,500		51,500

Note : It has been assumed that due to shortage of cash, bank overdraft of the required amount has been taken to make payment to *A*'s Executor's.

ILLUSTRATION 46.

Sita, Reeta and Geeta are partners in a firm sharing profits and losses in the ratio of 4 : 3 : 1. As per the terms of Partnership deed on the death of any partner, Goodwill of deceased partner was to be valued at 50% of the net profits credited to that Partner's Capital A/c during the last three completed years before her death. Sita died on 28th February 2022. The profits for the last five years were :

2017 — ₹60,000, 2018 — ₹97,000, 2019 — ₹1,05,000, 2020 — ₹30,000 and 2021 — ₹84,000

On the date of Sita's death, Building was found under valued by ₹80,000, which was to be considered. Calculate the amount of Sita's share of Goodwill in the firm and record the adjustment Journal Entries of Goodwill and revaluation of Building. The new profit sharing ratio between Reeta and Geeta will be equal.

SOLUTION:

Calculation of Sita's Share of Goodwill :

Total of last three years profit = ₹1,05,000 + ₹30,000 + ₹84,000 = ₹2,19,000

Sita's share in last three years profit $= ₹2,19,000 \times \frac{4}{8} = ₹1,09,500$

Sita's Share of Goodwill $= ₹1,09,500 \times \frac{50}{100} = ₹54,750$

Sita's Share of Goodwill will be contributed by Reeta and Geeta in their gaining ratio of 1 : 3 as under :

Reeta $= ₹54,750 \times \frac{1}{4} = ₹13,688$

Geeta $= ₹54,750 \times \frac{3}{4} = ₹41,062$

Calculation of Gaining Ratio :

Reeta $= \frac{1}{2} - \frac{3}{8} = \frac{4-3}{8} = \frac{1}{8}$

Geeta $= \frac{1}{2} - \frac{1}{8} = \frac{4-1}{8} = \frac{3}{8}$

Gaining Ratio $= \frac{1}{8} : \frac{3}{8} = 1 : 3$

JOURNAL ENTRIES

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
Feb. 28	Building A/c	Dr.		80,000	
	To Revaluation A/c				80,000
	(Increase in the value of Building)				
	Revaluation A/c	Dr.		80,000	
	To Sita's Capital A/c				40,000
	To Reeta's Capital A/c				30,000
	To Geeta's Capital A/c				10,000
	(Transfer of profit on revaluation to partners capital accounts in their old profit sharing ratio)				
	Reeta's Capital A/c	Dr.		13,688	
	Geeta's Capital A/c	Dr.		41,062	
	To Sita's Capital A/c				54,750
	(Sita's share of goodwill adjusted in the capital accounts of gaining partners in their gaining ratio of 1 : 3)				

ILLUSTRATION 47.

P, Q and *R* were partners in a firm sharing profits in 3 : 2 : 1. Following was their Balance Sheet as at 31st March, 2020 :

Liabilities		₹	*Assets*	₹
Creditors		76,000	Cash at Bank	26,000
Provision for Doubtful Debts		4,000	Debtors	80,000
Workmen's Compensation			Furniture	54,000
Reserve		1,00,000	Plant	90,000
Profit and Loss Account			Investments	
(for 2019-20)		90,000	(Market value 2,70,000)	2,00,000
Capitals :			Advertisement Expenditure	30,000
P	1,00,000		Patents	20,000
Q	80,000			
R	50,000	2,30,000		
		5,00,000		5,00,000

R died on 15th June 2020. It was found that

(*i*) Patents were valueless. Furniture was undervalued by 10% and Plant was overvalued by 20%.

(*ii*) There was a claim of ₹1,20,000 on account of workmen's compensation.

(*iii*) His executors were entitled to his share of profit upto his death based on last year's profit. Time period will be calculated in months.

Pass necessary journal entries for the above at the time of *R*'s death.

SOLUTION : JOURNAL

Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
2020				₹	₹
June 15	Furniture A/c	Dr.		6,000	
	Investments A/c	Dr.		70,000	
	To Revaluation A/c				76,000
	(Increase in the value of assets)				
	Revaluation A/c	Dr.		35,000	
	To Patents A/c				20,000
	To Plant A/c				15,000
	(Decrease in the value of assets)				
	Workmen Compensation Reserve A/c	Dr.		1,00,000	
	Revaluation A/c	Dr.		20,000	
	To Claim for Workmen Compensation A/c				1,20,000
	(Provision made for workmen claim)				
	Revaluation A/c	Dr.		21,000	
	To *P*'s Capital A/c				10,500
	To *Q*'s Capital A/c				7,000
	To *R*'s Capital A/c				3,500
	(Gain on revaluation distributed)				
	P's Capital A/c	Dr.		15,000	
	Q's Capital A/c	Dr.		10,000	
	R's Capital A/c	Dr.		5,000	

	To Advertisement Expenditure A/c (Advertisement expenditure written off)			30,000
	Profit & Loss A/c ... Dr. To *P*'s Capital A/c To *Q*'s Capital A/c To *R*'s Capital A/c (Profit distributed)		90,000	 45,000 30,000 15,000
	Profit & Loss Suspense A/c ... Dr. To *R*'s Capital A/c (Share of profit till the date of death)		3,125	 3,125
	R's Capital A/c ... Dr. To *R*'s Executor's A/c (Capital Account transferred to *R*'s Executor's A/c)		66,625	 66,625

Working Notes :

(*i*) Actual value of Furniture : $54{,}000 \times \frac{100}{90} = ₹60{,}000$

(*ii*) Actual value of Plant : $90{,}000 \times \frac{100}{120} = ₹75{,}000$

(*iii*) *R*'s share of profit till the date of his death : $90{,}000 \times \frac{2.5}{12} \times \frac{1}{6} = ₹3{,}125$

(*iv*) Total amount due to $R = 50{,}000 + 3{,}500 - 5{,}000 + 15{,}000 + 3{,}125 = ₹66{,}625$

ILLUSTRATION 48.

Naveen, Kavita and Vishesh were partners in a firm sharing profits and losses in the ratio of 5 : 4 : 1. Their Balance Sheet as at 31st March, 2019 was as follows :

BALANCE SHEET OF NAVEEN, KAVITA AND VISHESH
as at 31st March, 2019

Liabilities		*Amount*	*Assets*	*Amount*
		₹		₹
Capitals :			Plant and Machinery	5,50,000
Naveen	3,00,000		Stock	1,20,000
Kavita	2,00,000		Debtors	1,30,000
Vishesh	1,00,000	6,00,000	Cash	40,000
Profits for the year 2018-19		1,50,000	Advertisement Expenditure	20,000
Sundry Creditors		1,10,000		
		8,60,000		8,60,000

Naveen died on 30th June, 2019. According to the partnership deed, in addition to the deceased partner's capital, the executors are entitled to :

(*i*) His share in profits till the date of death on the basis of average profits of the last two years. The profit for the year 2017-18 was ₹50,000.

(*ii*) His share in the goodwill of the firm. Goodwill was to be calculated on the basis of two years' purchase of the average profits of the last two years.

Naveen withdrew ₹60,000 on 1st June, 2019.

Prepare Naveen's Capital Account which is to be rendered to his executor.

(C.B.S.E. 2020, Lucknow, Kolkata)

SOLUTION :

NAVEEN'S CAPITAL ACCOUNT

Dr. Particulars	Amount	Particulars	Amount Cr.
	₹		₹
To Drawings	60,000	By Balance b/d	3,00,000
To Advertisement Expenditure A/c	10,000	By Profit and Loss A/c	75,000
To Naveen's Executors A/c (Balancing Figure)	4,17,500	By P & L Suspense A/c[(1)]	12,500
		By Kavita's Capital A/c (4/5 of ₹1,00,000)	80,000
		By Vishesh's Capital A/c (1/5 of ₹1,00,000)	20,000
	4,87,500		4,87,500

Working Notes :

(1) Calculation of Share of Profit till the date of death :

	₹
Profit for 2017-18	50,000
Profit for 2018-19 (Given in Balance Sheet)	1,50,000
	2,00,000

Average Profit $= 2{,}00{,}000 \div 2 = ₹1{,}00{,}000$

Profit till the date of death $= 1{,}00{,}000 \times \frac{3}{12} = ₹25{,}000$

Naveen's Share $= 25{,}000 \times \frac{5}{10} = ₹12{,}500$

(2) Firm's Goodwill = Average Profit × Two Year's Purchase

$= 1{,}00{,}000 \times 2 = 2{,}00{,}000$

Naveen's Share $= 2{,}00{,}000 \times \frac{5}{10} = ₹1{,}00{,}000$

ILLUSTRATION 49.

D, E, F, P and *Z* were partners in a firm sharing profits in the ratio 5 : 4 : 3 : 2 : 1 respectively. Unfortunately, *P* and *Z* met with a tragic car accident in which both of them died.

The goodwill of the firm was valued at ₹1,50,000 and *D, E* and *F* decided to share future profits in the ratio of 4 : 6 : 5 respectively.

Give journal entry to record goodwill.

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	E's Capital A/c ($\frac{2}{15}$ of ₹1,50,000)	Dr.		20,000	

F's Capital A/c ($\frac{2}{15}$ of ₹1,50,000) Dr.		20,000	
To D's Capital A/c ($\frac{1}{15}$ of ₹1,50,000)			10,000
To P's Capital A/c ($\frac{2}{15}$ of ₹1,50,000)			20,000
To Z's Capital A/c ($\frac{1}{15}$ of ₹1,50,000)			10,000
(Sacrificing partner's goodwill borne by gaining partners E and F)			

Working Notes : (*i*) Calculation of Gaining Ratio :

	D	*E*	*F*	*P*	*Z*
New Ratio	$\frac{4}{15}$	$\frac{6}{15}$	$\frac{5}{15}$	—	—
Old Ratio	$\frac{5}{15}$	$\frac{4}{15}$	$\frac{3}{15}$	$\frac{2}{15}$	$\frac{1}{15}$
New Ratio – Old Ratio	$\frac{1}{15}$ (Sacrifice)	$\frac{2}{15}$ (Gain)	$\frac{2}{15}$ (Gain)	$\frac{2}{15}$ (Sacrifice)	$\frac{1}{15}$ (Sacrifice)

ILLUSTRATION 50.

A, *B* and *C* are partners sharing profits and losses equally. *A* dies on 1st April 2019. It was decided to value goodwill of the firm at three year's purchase of weighted average profits of the past four years.

The profits ended 31st March each year were : 2016 ₹1,00,000; 2017 ₹2,10,000; 2018 ₹1,60,000 and 2019 ₹2,50,000 and weights assigned were 2016-1; 2017 -2; 2018-3 and 2019-4.

You are informed that :

(*i*) Profits for the year ended 31st March 2016 were ascertained after charging loss on sale of machinery ₹50,000.

(*ii*) Repairs to Machinery amounting to ₹20,000 was wrongly debited to Machinery Account on 1st July 2017. Depreciation was charged on Machinery @ 10% p.a. on written down value basis.

(*iii*) *B* and *C* decided to share future profits in the ratio of 5 : 4.

You are required to pass necessary journal entry for goodwill on *A*'s death.

SOLUTION : Calculation of Adjusted Profits

	31st March 2016	*31st March 2017*	*31st March 2018*	*31st March 2019*
	₹	₹	₹	₹
Profits	1,00,000	2,10,000	1,60,000	2,50,000
Add : Loss on sale of Machinery	50,000			
Less : Repairs to Machinery			(20,000)	
Add : Depreciation wrongly debited to P & L A/c			1,500	1,850
	1,50,000	2,10,000	1,41,500	2,51,850

Years ending		Profits	Weights	Products
		₹		₹
31st March	2016	1,50,000	1	1,50,000
,,	2017	2,10,000	2	4,20,000
,,	2018	1,41,500	3	4,24,500
,,	2019	2,51,850	4	10,07,400
			10	20,01,900

Goodwill = Weighted Average Profit × No. of Year's Purchase

$= \dfrac{\text{Total Products}}{\text{Total Weight}} \times$ No. of Year's Purchase

$= \dfrac{20,01,900}{10} \times 3 = ₹6,00,570$

A's share of Goodwill $= 6,00,570 \times \dfrac{1}{3} = ₹2,00,190$

Gaining Ratio : Old Ratio among A, B and $C = 1 : 1 : 1$

New Ratio between B and $C = 5 : 4$

$B \text{ Gains} = \dfrac{5}{9} - \dfrac{1}{3} = \dfrac{5-3}{9} = \dfrac{2}{9}$

$C \text{ Gains} = \dfrac{4}{9} - \dfrac{1}{3} = \dfrac{4-3}{9} = \dfrac{1}{9}$

Gaining Ratio = 2 : 1

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019					
April 1	*B*'s Capital A/c	Dr.		1,33,460	
	C's Capital A/c	Dr.		66,730	
	To *A*'s Capital A/c				2,00,190
	(*A*'s share of goodwill debited to continuing partners in their gaining ratio of 2 : 1)				

ILLUSTRATION 51.

A and *B* are partners sharing profits in the ratio of *A* 5/10, *B* 3/10 and transfer to reserve 2/10. Their balance sheet as at 31st March, 2020 was as follows :

Liabilities		₹	Assets	₹
Sundry Creditors		16,000	Cash at Bank	10,800
Workmen Compensation Reserve		9,600	Sundry Debtors	20,000
Capitals :			Fixed Assets	1,00,000
A	80,000		Goodwill	15,000
B	40,200	1,20,200		
		1,45,800		1,45,800

B died on 1st April, 2020. Besides his capital and reserves, *B*'s legal representatives are entitled to his share of goodwill, based on the total profits of the last three years, which were ₹10,300; ₹15,100 and ₹13,600.

Assets were revalued as follows :

Fixed Assets ₹1,20,000; ₹2,000 out of debtors are bad and a provision of 5% is to be made for bad debts and 2% for discount on debtors. Prepaid insurance is ₹490 and outstanding salaries ₹3,000. There is an old typewriter not recorded in the books valued at ₹4,000.

Prepare Revaluation A/c and *B*'s A/c to be rendered to his legal representatives.

SOLUTION :

Working Note :

Total Goodwill = ₹10,300 + ₹15,100 + ₹13,600 = ₹39,000

B's Share of Goodwill = $39,000 \times \frac{3}{8}$ = ₹14,625

B's Share of Goodwill will be adjusted to *A*'s Capital Account.

REVALUATION A/C

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Debtors (Bad Debts)	2,000	By Fixed Assets	20,000
To Provision for Bad Debts	900	By Prepaid Insurance	490
To Provision for Discount	342	By Typewriter	4,000
To Outstanding salaries	3,000		
To Profits : *A*'s Capital A/c	11,405		
B's Capital A/c	6,843		
	24,490		24,490

B's CAPITAL A/C

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Goodwill (Written off)	5,625	By Balance b/d	40,200
To *B*'s Executor's A/c — — Balance transferred	59,643	By Workmen Compensation Reserve (Note 2)	3,600
		By *A*'s Capital A/c (Share of Goodwill)	14,625
		By Revaluation A/c	6,843
	65,268		65,268

2. Since there is no claim against Workmen's Compensation Reserve *B*'s share in this reserve is credited to his account.

ILLUSTRATION 52.

A, *B* and *C* were carrying on business with the following assets with effect from 1st April, 2018. Furniture ₹18,000; Machine ₹72,000; Cash ₹10,000; Debtors ₹20,000. Their profit-sharing ratio was 5 : 3 : 2. Capital is also shared in the same ratio. *B* died on 30th September, 2018. His son claimed his father's interest in the firm.

The following was the settlement :

(1) Allow his capital to his credit on the date of death.

(2) Give 5% p.a. interest on his capital.

(3) He had been drawing @ ₹600 per month which he withdrew at the beginning of each month. He be allowed to retain these drawings as a part of his share of profit.

(4) Interest @ 6% p.a. be charged on his drawings.

(5) Goodwill was evaluated twice the average of profits which were ₹21,000. Prepare *B*'s Personal Account.

SOLUTION:

I. Balance Sheet of the firm will have to be prepared in order to ascertain the Capitals of the partners.

BALANCE SHEET

Liabilities	₹	*Assets*	₹
Capital A/c (Balancing figure)	1,20,000	Cash	10,000
A 1,20,000 × $\frac{5}{10}$ = 60,000		Debtors	20,000
		Furniture	18,000
B 1,20,000 × $\frac{3}{10}$ = 36,000		Machine	72,000
C 1,20,000 × $\frac{2}{10}$ = 24,000			
	1,20,000		1,20,000

II. Goodwill = 21,000 × 2 = 42,000

B's share of Goodwill = 42,000 × $\frac{3}{10}$ = 12,600

B's share of Goodwill will be adjusted into the capital accounts of *A* and *C* in the gaining ratio of 5 : 2.

III. Interest on *B*'s Drawings :

On ₹600 for 6 months	=	3,600 Products
On ₹600 for 5 months	=	3,000 Products
On ₹600 for 4 months	=	2,400 Products
On ₹600 for 3 months	=	1,800 Products
On ₹600 for 2 months	=	1,200 Products
On ₹600 for 1 month	=	600 Products
		12,600

Interest = 12,600 × $\frac{6}{100}$ × $\frac{1}{12}$ = ₹63

Dr. *B*'s CAPITAL A/C Cr.

Particulars	₹	*Particulars*	₹
To Drawings	3,600	By Balance b/d	36,000
To Interest on drawings 6% on		By Int. on Capital	900
₹3,600 for $3\frac{1}{2}$ average months	63	By P & L Suspense A/c	3,600
		By *A*'s Capital (Goodwill)	9,000
To *B*'s Executor's A/c —		By C's Capital (Goodwill)	3,600
Balance transferred	49,437		
	53,100		53,100

ILLUSTRATION 53.

Following is the Balance Sheet of Pushpa, Rashi and Seema who are sharing profits in 2 : 1 : 2 as at March 31, 2018 :

Liabilities		₹	Assets	₹
Creditors		38,000	Goodwill	40,000
Employee's Provident Fund		2,000	Land & Building	2,00,000
Profit & Loss Account		60,000	Stock	65,000
Capitals :			Debtors	30,000
Pushpa	1,20,000		Cash and Bank	65,000
Rashi	80,000			
Seema	1,00,000	3,00,000		
		4,00,000		4,00,000

Pushpa died on June 12, 2018. According to partnership deed, the executors are entitled to :

(*i*) Her capital as per Balance Sheet;

(*ii*) Interest on capital @ 8% p.a. upto the date of death.

(*iii*) Her share of profit upto the date of death on the basis of average profits for the past 3 years.

(*iv*) Her share of goodwill valued on the basis of two times the average profits of the past 3 years.

Profits for the past three years were ₹30,000; ₹70,000 and ₹80,000 respectively. Rashi and Seema acquired Pushpa's share in the ratio of 1 : 5.

Prepare Pushpa's A/c to be rendered to her executor's. Also calculate the new profit sharing ratios.

SOLUTION:

Dr. PUSHPA'S CAPITAL A/C Cr.

Date	Particulars	₹	Date	Particulars	₹
2018			2018		
June 12	To Goodwill (Written off)	16,000	April 1	By Balance b/d	1,20,000
June 12	To Pushpa's Executor's A/c (Balance transferred)	1,82,720	June 12	By Profit & Loss A/c	24,000
			June 12	By Interest on Capital(1)	1,920
			June 12	By Rashi's Capital A/c(2) (Profit)	800
				By Seema's Capital A/c (Profit)	4,000
			June 12	By Rashi's Capital A/c (Goodwill)	8,000
			June 12	By Seema's Capital A/c (Goodwill)	40,000
		1,98,720			1,98,720

Calculation of new profit sharing ratio :

Pushpa's share $(\frac{2}{5})$ has been acquired by Rashi and Seema in the ratio of 1 : 5

Rashi will gain $\frac{1}{6}$ of $\frac{2}{5} = \frac{1}{15}$

Seema will gain $\frac{5}{6}$ of $\frac{2}{5}$ $= \frac{1}{3}$

Hence, Rashi's new share $= \frac{1}{5} + \frac{1}{15} = \frac{3+1}{15} = \frac{4}{15}$

Seema's new share $= \frac{2}{5} + \frac{1}{3} = \frac{6+5}{15} = \frac{11}{15}$

New Ratio of Rashi and Seema = 4 : 11

Working Notes :

(1) Interest on Capital :

Number of days from March 31 to June 12 = 73

Interest on Capital $= 1,20,000 \times \frac{8}{100} \times \frac{73}{365}$ = ₹ 1,920

(2) Share of Profit :

Average Profit $= \frac{30,000 + 70,000 + 80,000}{3}$ = ₹60,000

Pushpa's share upto the date of death $= 60,000 \times \frac{73}{365} \times \frac{2}{5}$ = ₹ 4,800

Note : This amount of ₹4,800 will be credited to Pushpa and debited to Rashi and Seema in their gaining ratio of 1 : 5. It should not be debited to Profit & Loss Suspense A/c because the profit sharing ratio of continuing partners, in between them, does not remain the same.

(3) Valuation of Goodwill :

Goodwill = Average Profit × 2

Goodwill = 60,000 × 2 = ₹1,20,000

Pushpa's share $= 1,20,000 \times \frac{2}{5}$ = ₹ 48,000

Rashi and Seema have gained in the ratio of 1 : 5

Hence, amount of goodwill debited to Rashi $= 48,000 \times \frac{1}{6}$ = ₹ 8,000

amount of goodwill debited to Seema $= 48,000 \times \frac{5}{6}$ = ₹40,000

ILLUSTRATION 54.

A, B and *C* were partners sharing profits in the proportion of one-half, one-fourth and one-fourth respectively. Their Balance Sheet as at 31st March, 2018 was as follows:

Liabilities	₹	*Assets*	₹
Sundry Creditors	40,000	Cash	10,000
A's Capital	1,00,000	Sundry Debtors	45,000
B's Capital	60,000	Stock-in-Trade	55,000
C's Capital	40,000	Loan to *A*	30,000
		Freehold Premises	1,00,000
	2,40,000		2,40,000

A died on 1st April, 2018. According to the partnership agreement, the goodwill was to be calculated at two years' purchase of average profits of three completed years preceding the death or retirement of a partner. The deceased partners' share of capital

and goodwill, etc., was paid out in cash on 4th April, 2018, the available cash balance being supplemented by a loan from firm's banker on the security of the freehold property. No interest to be allowed on intervening period of 2 months. The net profits of the years ending 31st March 2016, 2017 and 2018 were ₹55,000, ₹48,000 and ₹65,000 respectively.

You are required to show the Journal entries, the Capital Accounts of the partners and *A*'s Executor's Account.

SOLUTION:

JOURNAL ENTRIES

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2018					
April 1	*B*'s Capital A/c	Dr.		28,000	
	C's Capital A/c	Dr.		28,000	
	To *A*'s Capital A/c				56,000
	(*A*'s share of goodwill adjusted into the Capital A/cs of *B* and *C* in the gaining ratio *i.e.*, equally)				
April 1	*A*'s Capital A/c	Dr.		30,000	
	To *A*'s Loan A/c				30,000
	(Transfer of *A*'s Loan A/c to his Capital A/c)				
April 1	*A*'s Capital A/c	Dr.		1,26,000	
	To *A*'s Executor's A/c				1,26,000
	(Amount due to *A* transferred to his Executor's A/c)				
April 4	Bank A/c	Dr.(2)		1,16,000	
	To Bank Loan A/c				1,16,000
	(Loan taken from the bank)				
April 4	*A*'s Executors' A/c	Dr.		1,26,000	
	To Cash A/c				10,000
	To Bank A/c				1,16,000
	(Amount paid to *A*'s Executors)				

Notes : (1) Valuation of Goodwill :

		₹
Total Profit	55,000 + 48,000 + 65,000	1,68,000
Average Profit	$\frac{1,68,000}{3}$	56,000
Hence, Goodwill	56,000 × 2	1,12,000
A's share of Goodwill	$\frac{1,12,000}{2}$	56,000

(2) Calculation of Bank Loan :

	₹
Available Cash	10,000
(–) Amount required to pay off *A*'s Executors	1,26,000
Loan required	1,16,000

Dr. CAPITAL ACCOUNTS Cr.

Date	Particulars	*A*	*B*	*C*	Date	Particulars	*A*	*B*	*C*
		₹	₹	₹			₹	₹	₹
2018					2018				
April 1	To *A*'s				April 1	By Bal. b/d	1,00,000	60,000	40,000

	Capital A/c		28,000	28,000	April 1	By B's Capital A/c	28,000		
April 1	To A's Loan	30,000	—	—	April 1	By C's Capital A/c	28,000		
April 1	To A's Executors' A/c	1,26,000	—	—					
April 1	To Bal. c/d	—	32,000	12,000					
		1,56,000	60,000	40,000			1,56,000	60,000	40,000

Dr. **A's EXECUTOR'S ACCOUNT** Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2018			2018		
April 4	To Cash A/c	10,000	April 1	By A's Capital A/c	1,26,000
April 4	To Bank A/c	1,16,000			
		1,26,000			1,26,000

ILLUSTRATION 55.

On 31st March, 2022, the Balance Sheet of *P*, *Q* and *R* who were partners in a firm, was as under :

Liabilities		₹	*Assets*	₹
Sundry Creditors		21,000	Buildings	26,000
Employee's Provident Fund		4,000	Investment	15,000
Employee's Compensation Reserve		8,000	Debtors	15,000
Contingency Reserve		12,000	Bills Receivable	6,000
Capitals :			Stock	12,000
P	15,000		Cash	6,000
Q	10,000			
R	10,000	35,000		
		80,000		80,000

The partnership deed provides that the profits be shared in the ratio of 2 : 1 : 1 and that in the event of death of any partner, his executors will be entitled to be paid out :

(*a*) The capital to his credit at the date of last Balance Sheet;

(*b*) His proportion of Reserve at the date of last Balance Sheet;

(*c*) His proportion of profits to the date of death based on the average profits of the last three completed years, plus 10%, and

(*d*) By way of goodwill, his proportion of the total profits for the three preceding years.

(*e*) The net profit for the last three years ending 31st March were :

2020	₹16,000
2021	₹16,000
2022	₹15,400

R died on 1st July, 2022. He had withdrawn ₹5,000 to the date of his death. The investments were sold at par and *R*'s executors were paid off.

Prepare Partners' Capital Accounts, *R*'s Executor's Account and Balance Sheet of the surviving partners *P* and *Q*.

SOLUTION :

PARTNERS' CAPITAL ACCOUNTS

Dr. Cr.

Particulars	*P*	*Q*	*R*	*Particulars*	*P*	*Q*	*R*
	₹	₹	₹		₹	₹	₹
To *R*'s Capital A/c (Share of Goodwill)	7,900	3,950	—	By Balance b/d	15,000	10,000	10,000
To Bank A/c (Drawings)	—	—	5,000	By Employee's Compensation Reserve	4,000	2,000	2,000
To *R*'s Executors	—	—	22,936	By Contingency Reserve	6,000	3,000	3,000
To Balance c/d	17,100	11,050	—	By P & L Suspense A/c (See Note 1)	—	—	1,086
				By *P*'s Capital A/c (Share of goodwill)	—	—	7,900
				By *Q*'s Capital A/c (Share of goodwill)	—	—	3,950
	25,000	15,000	27,936		25,000	15,000	27,936

R'S EXECUTOR'S ACCOUNT

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Bank A/c	22,936	By *R*'s Capital A/c	22,936
	22,936		22,936

BALANCE SHEET OF *P* AND *Q*

as at 1st July, 2022

Liabilities		₹	*Assets*	₹
Sundry Creditors		21,000	Buildings	26,000
Employee's Provident Fund		4,000	Debtors	15,000
Bank Loan(3)		6,936	Bills Receivable	6,000
Capitals :			Stock	12,000
P	17,100		Profit & Loss Suspense A/c	1,086
Q	11,050	28,150		
		60,086		60,086

Working Notes :

(1) Ascertainment of *R*'s share of profit :

Total profits for the last three years = ₹16,000 + ₹16,000 + ₹15,400
= ₹47,400

Average Profits = $\frac{₹47,400}{3}$ = ₹15,800

Profit (From 1st April, 2022 to 1st July, 2022) = ₹15,800 × $\frac{3}{12}$ = ₹3,950

			₹
R's share in Profit	= ₹3,950 × $\frac{1}{4}$	=	987
Add : 10% of ₹987		=	99
		=	1,086

(2) *R*'s Share of Goodwill :

Total profits for the three preceding years = ₹47,400

R's share of profit (Goodwill) = ₹47,400 × $\frac{1}{4}$ = ₹11,850

R's share of goodwill = ₹11,850, which is contributed by *P* and *Q* in the ratio of 2 : 1.

(3) Calculation of Bank Loan :

	₹
Available Cash	6,000
(+) Received from sale of Investments	15,000
	21,000
(–) Withdrew by *R* to the date of his death (Drawings)	5,000
	16,000
(–) Amount required to pay off *R*'s Executors	22,936
Loan Required	6,936

Alternatively, a Bank Account may be prepared to ascertain the amount of bank loan :

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Cash A/c	6,000	By *R*'s Capital A/c (Drawings)	5,000
To Investments A/c	15,000	By *R*'s Executor's A/c	22,936
To Bank Loan (Balancing Figure)	6,936		
	27,936		27,936

ILLUSTRATION 56.

A, *B* and *C* are partners sharing profits of 2 : 1 : 1. They closed their books on 31st March each year. *A* died on 31st May, 2022. *B* and *C* decided to share future profits in 3 : 2. On this date, their Balance Sheet was as follows :

Liabilities		₹	*Assets*	₹
Creditors		37,900	Bank Balance	2,00,000
Profit for 2 months (before interest & salaries)		31,100	Sundry Debtors	39,000
Capitals :			Loan to *A*	40,000
A	1,00,000			
B	60,000			
C	50,000	2,10,000		
		2,79,000		2,79,000

According to the partnership deed :

(a) Interest on capital is allowed @ 6% p.a. *A* and *B* are entitled to salaries at ₹3,000 and ₹2,500 p.m.

(b) In the event of death of a partner goodwill was to be valued at 2 years' purchase of the average net profits of 3 completed years preceding death. The net profits for the years ending 31st March 2020, 2021 and 2022 were ₹55,000, ₹48,000 and ₹65,000 respectively.

A's share was paid to his executors. *B* and *C* continued the firm.

Prepare Profit & Loss A/c, Partners' Capital A/cs, and Balance Sheet of *B* and *C*.

SOLUTION : PROFIT AND LOSS APPROPRIATION ACCOUNT

for the period ended 31st May, 2022

Dr. Cr.

Particulars		₹	*Particulars*	₹
To Interest on Capitals :			By Profit & Loss A/c	31,100
(for 2 months)			(being profit for 2 months)	
A	1,000			
B	600			
C	500	2,100		
To Salary (for 2 months)				
A	6,000			
B	5,000	11,000		
To Profit transferred to :				
A's Capital A/c	9,000			
B's Capital A/c	4,500			
C's Capital A/c	4,500	18,000		
		31,100		31,100

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To *A*'s Capital A/c		39,200	16,800	By Balance b/d	1,00,000	60,000	50,000
To *A*'s Loan A/c	40,000			By Int. on Capital	1,000	600	500
To Balance transferred to *A*'s executor's A/c	1,32,000			By Salary	6,000	5,000	—
				By P & L App. A/c	9,000	4,500	4,500
To Balance c/d		30,900	38,200	By *B*'s Capital A/c	39,200		
				By *C*'s Capital A/c	16,800		
	1,72,000	70,100	55,000		1,72,000	70,100	55,000

Dr. *A*'s EXECUTOR'S ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Bank A/c	1,32,000	By *A*'s Capital A/c	1,32,000

BALANCE SHEET OF *B* AND *C*

as at 31st May, 2022

Liabilities	₹	*Assets*	₹
Creditors	37,900	Bank Balance	
Capitals :		(2,00,000 – 1,32,000)	68,000
B	30,900	Sundry Debtors	39,000
C	38,200		
	1,07,000		1,07,000

Working Note :

Goodwill : Average Profits $= \frac{55,000 + 48,000 + 65,000}{3} = ₹56,000$

Goodwill at 2 years purchase $=$ ₹$56,000 \times 2 =$ ₹$1,12,000$

A's share of goodwill $=$ ₹$1,12,000 \times \frac{2}{4} =$ ₹$56,000$

A's share of goodwill will be adjusted into the Capital A/cs of *B* and *C* in their gaining ratio of 7 : 3.

ILLUSTRATION 57.

The following was the Balance Sheet of Om & Co. in which *X, Y* and *Z* were partners sharing profits and losses in the ratio of 1 : 2 : 2 as at 31.3.2017 :

BALANCE SHEET

as at 31.3.2017

Liabilities		₹	*Assets*	₹
Sundry Creditors		20,000	Goodwill	30,000
Bank Loan		50,000	Building	1,20,000
General Reserve		30,000	Computers	80,000
Capital Accounts :			Stock	20,000
X	40,000		Sundry Debtors	20,000
Y	80,000		Cash at Bank	20,000
Z	80,000	2,00,000	Investments	10,000
		3,00,000		3,00,000

Mr. *Z* died on 31st December, 2017. His account has to be settled under the following terms :

Goodwill is to be calculated at the rate of two years' purchase on the basis of average of last three years' profits and losses. The profits and losses for the three years were as detailed below :

Year ending on	*Profit (loss)*
	₹
31.3.2017	30,000
31.3.2016	20,000
31.3.2015	(10,000)

Profit for the period from 1.4.2017 to 31.12.2017 shall be ascertained proportionately on the basis of average profits and losses of the preceding three years.

During the year ending on 31.3.2017 a car costing ₹40,000 was purchased on 1.4.2016 and debited to travelling expenses account on which depreciation is to be calculated at 20% p.a. This asset is to be brought into account at the depreciated value.

Values of other assets were agreed as follows :

Building at ₹1,36,000, Computers at ₹50,000, Investments at ₹6,000. Debtors are considered good.

You are asked to prepare Capital Accounts and Balance Sheet of the firm Om & Co. as at 31.12.2017 transferring the amount due to Z to his Executor's Account.

It may be assumed that other items of assets and liabilities remained the same.

SOLUTION :

(*i*) Adjusted Profit for the year ending 31.3.2017 :

		₹
Profit as per Accounts		30,000
Add : Purchase of Car wrongly debited to Travelling Expenses	40,000	
Less : Depreciation @ 20%	8,000	32,000
		62,000

(*ii*) Valuation of Goodwill :

Year ending on	Profit/Loss ₹
31.3.2015 (Loss)	(10,000)
31.3.2016 (Profit)	20,000
31.3.2017 (Profit)[1]	62,000
Total for 3 years	72,000
Average Profit : 72,000 ÷ 3	24,000

Value of Goodwill at 2 year's purchase = 24,000 × 2 = 48,000

Z's share = $48{,}000 \times \frac{2}{5} = 19{,}200$

Adjustment Entry for Goodwill :

X's Capital A/c (1/3 of 19,200)	Dr.	6,400	
Y's Capital A/c (2/3 of 19,200)	Dr.	12,800	
To Z's Capital A/c			19,200

(*iii*) Z's share of profit for 9 months upto the date of death :

Average Profit [as calculated in (*ii*) above] = ₹24,000

Profit for 9 months = $24{,}000 \times \frac{9}{12}$ = ₹18,000

Z's share therein = $18{,}000 \times \frac{2}{5}$ = ₹ 7,200

Adjustment Entry :

Profit & Loss Suspense A/c	Dr.	7,200	
To Z's Capital A/c			7,200

(*iv*)

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Computers A/c	30,000	By Building A/c	16,000

		₹		₹
To Investments A/c		4,000	By Motor Car A/c (40,000 – 8,000)	32,000
To Profit transferred to :				
X's Capital A/c 1/5	2,800			
Y's Capital A/c 2/5	5,600			
Z's Capital A/c 2/5	5,600	14,000		
		48,000		48,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	X	Y	Z	Particulars	X	Y	Z
	₹	₹	₹		₹	₹	₹
To Goodwill (Written off)	6,000	12,000	12,000	By Balance b/d	40,000	80,000	80,000
To Z's Capital A/c (Adjustment for Goodwill)	6,400	12,800		By Gen. Reserve	6,000	12,000	12,000
To Z's Executor's A/c			1,12,000	By Revaluation A/c	2,800	5,600	5,600
To Balance c/d	36,400	72,800		By X's Capital A/c (Adjustment for Goodwill)			6,400
				By Y's Capital A/c (Adjustment for Goodwill)			12,800
				By P & L Suspense A/c			7,200
	48,800	97,600	1,24,000		48,800	97,600	1,24,000

BALANCE SHEET *as at 31st Dec. 2017*

Liabilities		₹	*Assets*	₹
Sundry Creditors		20,000	Building	1,36,000
Bank Loan		50,000	Computers	50,000
Z's Loan A/c		1,12,000	Motor Car	32,000
Capital Accounts :			Investments	6,000
X	36,400		Stock	20,000
Y	72,800	1,09,200	Sundry Debtors	20,000
			Cash at Bank	20,000
			Profit & Loss Suspense A/c	7,200
		2,91,200		2,91,200

ILLUSTRATION 58.

Albert, Boris and Cyril are partners sharing profits and losses in the ratio of 3 : 2 : 1 and their balance sheet as at 31st March 2018 stood as under :

Liabilities	₹	*Assets*	₹
Albert's Capital	50,000	Building	70,000
Boris's Capital	50,000	Machinery	25,000
Cyril's Capital	50,000	Stock	32,000

Creditors	17,000	Debtors	15,000
		Bank	25,000
	1,67,000		1,67,000

Albert died on 1st July 2018 and the following decisions were taken by the surviving partners. According to the partnership deed his executors were entitled to :

(a) The deceased partner's capital as appearing in the last balance sheet and interest thereon at 6% per annum upto the date of death.

(b) His share of profit for the period he was alive based on the figure of 31st March, 2018.

(c) Goodwill according to his share of profit to be calculated by taking twice the amount of the average profit of the last three years. The profits of the previous years were :

31st March 2018	—	₹11,000
31st March 2017	—	₹15,000, and
31st March 2016	—	₹10,000.

(d) Assets were to be revalued :

Building	—	₹80,000
Stock	—	₹30,000, and
Provision for bad debts @ 10%		

Assuming that all the above changes are to be incorporated in the new firm and are not to be written off (except goodwill) prepare the Revaluation Account, Partners Capital Accounts and a Balance Sheet as at 1st July, 2018.

SOLUTION.

Books of Albert, Boris and Cyril

REVALUATION ACCOUNT

Dr. Cr.

Particulars		₹	*Particulars*	₹
1.7.2018			*1.7.2018*	
To Stock A/c		2,000	By Building A/c	10,000
To Provision for Bad Debts A/c		1,500		
To Profit on Revaluation :				
Albert's Capital A/c (3/6)	3,250			
Boris's Capital A/c (2/6)	2,167			
Cyril's Capital A/c (1/6)	1,083	6,500		
		10,000		10,000

CAPITAL ACCOUNTS

Dr. Cr.

Particulars	*Albert*	*Boris*	*Cyril*	*Particulars*	*Albert*	*Boris*	*Cyril*
1.7.2018	₹	₹	₹	*1.4.2018*	₹	₹	₹
To Albert Capital A/c (Goodwill)		8,000	4,000	By Balance b/d	50,000	50,000	50,000
				1.7.2018			

To Executors of Albert A/c — transfer	67,375	—	—	By Profit & Loss Suspense A/c : Interest on Capital	750	—	—
To Balance c/d	—	44,167	47,083	Share of Profit $(11,000 \times \frac{3}{12} \times \frac{3}{6})$	1,375		
				By Boris Capital A/c (Goodwill)	8,000		
				By Cyril Capital A/c (Goodwill)	4,000		
				By Revaluation A/c — Profit	3,250	2,167	1,083
	67,375	52,167	51,083		67,375	52,167	51,083

Boris and Cyril

BALANCE SHEET *as at 1st July, 2018*

Liabilities		₹	*Assets*		₹
Capital Accounts :			Building		80,000
Boris	44,167		Machinery		25,000
Cyril	47,083	91,250	Stock		30,000
Executors of Albert		67,375	Debtors	15,000	
Creditors		17,000	*Less* : Provision for Bad Debts	1,500	13,500
			Bank		25,000
			Profit & Loss Suspense A/c		2,125
		1,75,625			1,75,625

Working Notes :

(1) Albert's share of Goodwill :

Average profits of last 3 years : $\frac{1}{3} \times ₹(11,000 + 15,000 + 10,000)$ = ₹12,000

Albert's share of average profits : $\frac{3}{6} \times ₹12,000$ = ₹ 6,000

Value of his share of goodwill : $2 \times ₹6,000$ = ₹12,000

(2) Due to lack of adequate information current assets and current liabilities on 1.7.2018 have been assumed to have remained the same as they were on 31.3.2018. In actual practice, however these will be different.

ILLUSTRATION 59.

X, *Y* and *Z* were partners sharing profits and losses in the ratio of 5 : 3 : 2 respectively. On 31st March, 2018 their balance sheet stood as under :

Liabilities	₹	*Assets*	₹
Sundry Creditors	27,500	Goodwill	12,500
Reserve Fund	10,000	Building	50,000
Workmen's Compensation Reserve	5,000	Patents	15,000

Capital A/cs			Machinery	75,000
X	75,000		Stock	25,000
Y	62,500		Debtors	20,000
Z	37,500	1,75,000	Bank	20,000
		2,17,500		2,17,500

Adjustments :

Z died on 1st August 2018, it was agreed that :

(a) Goodwill be valued at $2\frac{1}{2}$ years purchase of the average profits of last four years, which were — 2014-15 ₹32,500; 2015-16 ₹30,000; 2016-17 ₹40,000 and 2017-18 ₹37,500.

(b) Machinery be valued at ₹70,000; Patents at ₹20,000 and Buildings at ₹62,500.

(c) For the purpose of calculating Z's share in profits upto the date of his death, the profits in 2018-19 should be taken to have been earned on the same scale as in 2017-18.

(d) A sum of ₹10,500 is to be paid immediately to the executor's of Z and the balance to be paid in four equal half-yearly instalments together with interest @ 10% p.a.

Prepare Journal entries to record the transactions and Z's Capital A/c and Executor's A/c for 2018-19.

SOLUTION : JOURNAL ENTRIES

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2018					
August 1	X's Capital A/c	Dr.		6,250	
	Y's Capital A/c	Dr.		3,750	
	Z's Capital A/c	Dr.		2,500	
	To Goodwill A/c				12,500
	(Goodwill written off)				
August 1	X's Capital A/c	Dr.		10,938	
	Y's Capital A/c	Dr.		6,562	
	To Z's Capital A/c				17,500
	(Z's share of goodwill adjusted into the Capital A/cs of X and Y in their gaining ratio of 5 : 3)				
August 1	Reserve Fund A/c	Dr.		10,000	
	To X's Capital A/c				5,000
	To Y's Capital A/c				3,000
	To Z's Capital A/c				2,000
	(Reserve Fund transferred to capital accounts of partners in the ratio of 5 : 3 : 2)				
August 1	Workmen's Compensation Reserve A/c	Dr.		5,000	
	To X's Capital A/c				2,500
	To Y's Capital A/c				1,500
	To Z's Capital A/c				1,000
	(Workmen's Compensation Reserve transferred to capital accounts in the ratio of 5 : 3 : 2)				

August 1	Revaluation A/c To Machinery A/c (Value of machinery reduced on revaluation)	Dr.	5,000	5,000
August 1	Patents A/c Building A/c To Revaluation A/c (Increase in the value of patents and building)	Dr. Dr.	5,000 12,500	17,500
August 1	Revaluation A/c To X's Capital A/c To Y's Capital A/c To Z's Capital A/c (Profit on revaluation transferred to partner's capital A/cs)	Dr.	12,500	6,250 3,750 2,500
August 1	Profit & Loss Suspense A/c To Z's Capital A/c (Transfer of $\frac{2}{10}$th share of profit upto 1st August, 2018 *i.e.*, $37,500 \times \frac{2}{10} \times \frac{4}{12}$)	Dr.	2,500	2,500
August 1	Z's Capital A/c To Z's Executor's A/c (Amount due to Z transferred to his Executor's A/c)	Dr.	60,500	60,500
August 1	Z's Executor's A/c To Bank A/c (Amount paid immediately)	Dr.	10,500	10,500

Dr. Z's CAPITAL A/C Cr.

Date	Particulars	₹	Date	Particulars	₹
2018			2018		
Aug. 1	To Goodwill A/c	2,500	April 1	By Balance b/d	37,500
Aug. 1	To Z's Executor's A/c	60,500	Aug. 1	By X's Capital A/c (Goodwill)	10,938
				By Y's Capital A/c (Goodwill)	6,562
			Aug. 1	By Reserve Fund A/c	2,000
			Aug. 1	By Workmen's Compensation Reserve	1,000
			Aug. 1	By Revaluation A/c	2,500
			Aug. 1	By Profit & Loss Suspense A/c (Share of Profit)	2,500
		63,000			63,000

Dr. Z's EXECUTOR'S A/C Cr.

Date	Particulars	₹	Date	Particulars	₹
2018			2018		
Aug. 1	To Bank A/c	10,500	Aug. 1	By Z's Capital A/c	60,500

2019 Feb. 1	To Bank A/c (¼ th of ₹50,000 + Interest ₹2,500)	15,000	2019 Feb. 1	By Interest A/c (10% p.a. on ₹50,000 for 6 months)	2,500
Feb. 1	To Balance c/d	37,500			
		63,000			63,000
2019 Mar. 31	To Balance c/d	38,125	2019 Feb. 1	By Balance b/d	37,500
			Mar. 31	By Interest A/c* (10% p.a. on ₹37,500 for 2 months)	625
		38,125			38,125

* ₹625 is the amount of interest accrued but not due.

Valuation of Goodwill :

				₹
Total Profit	=	32,500 + 30,000 + 40,000 + 37,500	=	1,40,000
Average Profit	=	1,40,000 ÷ 4	=	35,000
Hence, Goodwill	=	$35,000 \times \frac{5}{2}$	=	87,500
Z's share of Goodwill	=	$87,500 \times \frac{2}{10}$	=	17,500

ILLUSTRATION 60 (A).

A, *B* and *C* were partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. *C* died on 30th June, 2016. After all the necessary adjustments, his capital account showed a credit balance of ₹70,600. *C*'s executor was paid ₹10,600 on 1st July, 2016 and the balance in three equal yearly instalments starting from 30th June, 2017 with interest @10% p.a. on the unpaid amount. The firm closes its books on 31st March every year.

Prepare *C*'s Executor's Account till the amount is finally paid.

(C.B.S.E. 2019, Comptt.)

SOLUTION :

Dr. **C's Executors Account** Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2016 July 1	To Bank A/c	10,600	2016 June 30	By C's Capital A/c	70,600
2017 Mar. 31	To Balance c/d	64,500	2017 Mar. 31	By Interest	4,500
		75,100			75,100
2017 June 30	To Bank A/c (₹20,000 + ₹4,500 +₹1,500	26,000	2017 April 1	By Balance b/d	64,500
			June 30	By Interest	1,500
			2018		

2018 Mar. 31	To Balance c/d	43,000	Mar. 31	By Interest	3,000
		69,000			69,000
2018 June 30	To Bank A/c (20,000 + 3,000 + 1,000)	24,000	2018 April 1	By Balance b/d	43,000
			June 30	By Interest	1,000
2019 Mar. 31	To Balance c/d	21,500	2019 Mar. 31	By Interest	1,500
		45,500			45,500
2019 June 30	To Bank A/c (20,000 + 1,500 + 500)	22,000	2019 April 1	By Balance b/d	21,500
			June 30	By Interest	500
		22,000			22,000

ILLUSTRATION 60 (B).

Following is the Balance Sheet of *A, B* and *C* as at 31st March, 2015 :

Liabilities	₹	*Assets*	₹
Sundry Creditors	18,000	Tools	6,000
Workmen Compensation Reserve	19,200	Furniture	48,000
Capital Accounts :		Stock	36,000
A	60,000	Debtors	36,000
B	30,000	Cash at Bank	30,000
C	30,000	Cash in hand	1,200
	1,57,200		1,57,200

B died on 30th June 2015. Under the partnership agreement the executor of *B* was entitled to :

(*a*) Amount standing to the credit of his Capital Account.

(*b*) Interest on Capital which amounted to ₹375

(*c*) His share of goodwill ₹21,000.

(*d*) His share of profit from the closing of the last financial year to the date of death which amounted to ₹2,625.

B's executor was paid ₹20,400 on 1st July 2015 and the balance in four equal yearly instalments starting from 30th June, 2016 with interest @ 6% p.a.

Pass the necessary Journal entries and draw up *B*'s Account to be rendered to his executor and *B*'s Executor's Account till it is finally paid. The firm closes its books on 31st March every year.

SOLUTION:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2015 June 30	Workmen Compensation Reserve A/c	Dr.		6,400	
	To *B*'s Capital A/c				6,400
	(Transfer of *B*'s share of reserve to his Capital A/c)				
June 30	Interest on Capital A/c	Dr.		375	
	To *B*'s Capital A/c				375
	(Interest credited to his Capital A/c)				
June 30	*A*'s Capital A/c	Dr.		10,500	
	C's Capital A/c	Dr.		10,500	
	To *B*'s Capital A/c				21,000
	(Adjustment of *B*'s share of goodwill into the Capital A/cs of *A* and *C* in their gaining ratio *i.e.*, equally)				
June 30	P & L Suspense A/c	Dr.		2,625	
	To *B*'s Capital A/c				2,625
	(Transfer of profit till his death)				
June 30	*B*'s Capital A/c	Dr.		60,400	
	To *B*'s Executor's A/c				60,400
	(Amount due to *B* transferred to his Executor's A/c)				
July 1	*B*'s Executor's A/c	Dr.		20,400	
	To Bank A/c				20,400
	(Amount paid to *B*'s Executor)				

Dr. *B*'s CAPITAL A/C Cr.

Date	Particulars	₹	Date	Particulars	₹
2015			2015		
June 30	To *B*'s Executor's A/c (Balance transferred)	60,400	April 1	By Balance b/d	30,000
			June 30	By Workmen Compensation Reserve	6,400
			June 30	By Interest on Capital	375
			June 30	By *A*'s Capital A/c	10,500
			June 30	By *C*'s Capital A/c	10,500
			June 30	By P & L Suspense A/c	2,625
		60,400			60,400

Dr. *B*'s EXECUTOR'S A/C Cr.

Date	Particulars	₹	Date	Particulars	₹
2015			2015		
July 1	To Bank A/c	20,400	June 30	By *B*'s Capital A/c	60,400
2016			2016		
March 31	To Balance c/d	41,800	March 31	By Interest A/c (60,400 – 20,400)	

				$40,000 \times \frac{6}{100} \times \frac{9}{12}$	1,800
		62,200			62,200
2016 June 30	To Bank A/c (10,000 + 1,800 + 600)	12,400	2016 April 1	By Balance b/d	41,800
			June 30	By Interest A/c $40,000 \times \frac{6}{100} \times \frac{3}{12}$	600
2017 March 31	To Balance c/d	31,350	2017 March 31	By Interest A/c $30,000 \times \frac{6}{100} \times \frac{9}{12}$	1,350
		43,750			43,750
2017 June 30	To Bank A/c (10,000 + 1,350 + 450)	11,800	2017 April 1	By Balance b/d	31,350
			June 30	By Interest A/c $30,000 \times \frac{6}{100} \times \frac{3}{12}$	450
2018 March 31	To Balance c/d	20,900	2018 March 31	By Interest A/c $20,000 \times \frac{6}{100} \times \frac{9}{12}$	900
		32,700			32,700
2018 June 30	To Bank A/c (10,000 + 900 + 300)	11,200	2018 April 1	By Balance b/d	20,900
			June 30	By Interest A/c $20,000 \times \frac{6}{100} \times \frac{3}{12}$	300
2019 March 31	To Balance c/d	10,450	2019 March 31	By Interest A/c $10,000 \times \frac{6}{100} \times \frac{9}{12}$	450
		21,650			21,650
2019 June 30	To Bank A/c (10,000 + 450 + 150)	10,600	2019 April 1	By Balance b/d	10,450
			June 30	By Interest A/c $10,000 \times \frac{6}{100} \times \frac{3}{12}$	150
		10,600			10,600

Notes: (1) The date of closing the accounts is 31st March and the date of payment of instalments is 30th June.

(2) Total amount due to *B*'s Executor's is ₹40,000 payable in 4 instalments. Hence, yearly instalment = 40,000 ÷ 4 = ₹10,000 plus interest.

Accounting Treatment of Accumulated Profits/Losses when partners do not want to distribute them :

ILLUSTRATION 61.

On 31st March, 2022, *A*, *B* and *C* were sharing profits in the ratio of 5 : 3 : 2. On this date *A* retires and *B* and *C* decided to share future profits and losses in the ratio of 7 : 3. Their Balance Sheet disclosed the following items :

Reserve Fund	₹1,50,000
Profit & Loss (Cr. Balance)	₹ 90,000

Partners decide that *A*'s share of reserve and profit is to be adjusted into the accounts of *B* and *C*. You are required to give the adjusting entry.

SOLUTION :

Adjustment to be made for :

Reserve Fund	₹1,50,000
Profit & Loss	₹ 90,000
	₹2,40,000

Calculation of Gaining Ratios : (New Ratio – Old Ratio)

$$B = \frac{7}{10} - \frac{3}{10} = \frac{4}{10}$$

$$C = \frac{3}{10} - \frac{2}{10} = \frac{1}{10}$$

Thus, Gaining Ratio : 4 : 1.

Adjustment Entry :

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
March 31	*B*'s Capital A/c $(1,20,000 \times \frac{4}{5})$	Dr.		96,000	
	C's Capital A/c $(1,20,000 \times \frac{1}{5})$	Dr.		24,000	
	To *A*'s Capital A/c $(2,40,000 \times \frac{5}{10})$				1,20,000
	(*A*'s share of reserve and profit adjusted into the accounts of *B* and *C* in their gaining ratio)				

ILLUSTRATION 62.

P, *Q* and *R* were partners sharing profits and losses in the ratio of 5 : 4 : 3. Their Fixed Capitals were : *P* ₹4,00,000; *Q* ₹3,00,000 and *R* ₹2,00,000. *Q* retires and *P* and *R* decide to share future profits and losses in the ratio of 3 : 2. On this date, their Balance Sheet disclosed the following items :

	₹
Advertisement Suspense A/c	50,000
Dr. Balance of Profit & Loss A/c	1,30,000

It was decided to adjust Q's share of loss into the capital accounts of P and R. Give the necessary journal entry.

SOLUTION :

Adjustment to be made :

	₹
Advertisement Suspense A/c	50,000
Dr. Balance of Profit & Loss A/c	1,30,000
Total Loss	1,80,000

Calculation of Gaining Ratios : (New Ratio – Old Ratio)

$$P = \frac{3}{5} - \frac{5}{12} = \frac{36-25}{60} = \frac{11}{60}$$

$$R = \frac{2}{5} - \frac{3}{12} = \frac{24-15}{60} = \frac{9}{60} \text{ or } 11:9$$

Adjustment Entry :

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Q's Current A/c $(1{,}80{,}000 \times \frac{4}{12})$	Dr.		60,000	
	To P's Current A/c $(60{,}000 \times \frac{11}{20})$				33,000
	To R's Current A/c $(60{,}000 \times \frac{9}{20})$				27,000
	(Adjustment of Q's share of loss into the capital accounts of P and R in their gaining ratio)				

ILLUSTRATION 63.

Laxman, Mohan and Naresh are three partners sharing profits and losses in the ratio of 2 : 2 : 1. Mohan retires and the new ratio between Laxman and Naresh is agreed at 3 : 1. Following balances appeared in their books on the date of retirement :

	₹
Profit & Loss Balance (Dr.)	80,000
General Reserve	2,00,000
Advertisement Suspense Account	30,000

On this date Goodwill of the firm is valued at ₹60,000.

Continuing partners decided to record the effect of retirement without affecting the book value of above items. You are required to give the necessary journal entry.

SOLUTION :

Calculation of Net Effect of Accumulated Profits/Losses :

			₹
General Reserve			2,00,000
Less :	Profit & Loss A/c Dr. Balance	80,000	
	Advertisement Suspense Account	30,000	1,10,000
Net Accumulated Profit			90,000
Add : Value of Goodwill			60,000
			1,50,000

Gaining Ratio = New Ratio – Old Ratio

Laxman : $\frac{3}{4} - \frac{2}{5} = \frac{15-8}{20} = \frac{7}{20}$

Naresh : $\frac{1}{4} - \frac{1}{5} = \frac{5-4}{20} = \frac{1}{20}$ or 7 : 1

Adjustment Entry :

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Laxman's Capital A/c $(60,000 \times \frac{7}{8})$	Dr.		52,500	
	Naresh's Capital A/c $(60,000 \times \frac{1}{8})$	Dr.		7,500	
	To Mohan's Capital A/c $(1,50,000 \times \frac{2}{5})$				60,000
	(Adjustment of Mohan's share of accumulated profit and goodwill into the accounts of continuing partners in their gaining ratio)				

ILLUSTRATION 64.

A, *B* and *C* are partners sharing profits and losses in the ratio of 5 : 3 : 2. *C* retires on 31st March, 2022. An extract of their Balance Sheet on this date is given below :

Liabilities	₹	Assets	₹
Workmen Compensation Reserve	1,00,000		

A and *B* agreed that the book value of any item appearing in the Balance Sheet is not to be altered and any adjustment on the retirement of *C* is to be made by passing a single journal entry. Show the accounting treatment under the following alternative cases :

Case 1. If there is no other information

Case 2. If a claim for Workmen Compensation is estimated at ₹60,000

Case 3. If a claim for Workmen Compensation is estiamted at ₹1,00,000

Case 4. If a claim for Workmen Compensation is estimated at ₹1,50,000

SOLUTION :

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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
Case 1	*A*'s Capital A/c $(20,000 \times \frac{5}{8})$	Dr.		12,500	
	B's Capital A/c $(20,000 \times \frac{3}{8})$	Dr.		7,500	
	To *C*'s Capital A/c $(1,00,000 \times \frac{2}{10})$				20,000
	(Adjustment for *C*'s share of workmen Compensation reserve in gaining ratio of 5 : 3)				

Case 2	A's Capital A/c $(8,000 \times \frac{5}{8})$	Dr.	5,000	
	B's Capital A/c $(8,000 \times \frac{3}{8})$	Dr.	3,000	
	To C's Capital A/c $(40,000 \times \frac{2}{10})$			8,000
	(Adjustment for C's share of workmen compensation reserve of ₹1,00,000 *less* claim ₹60,000 in gaining ratio of 5 : 3)			
Case 3	No Entry			
Case 4	C's Capital A/c $(50,000 \times \frac{2}{10})$	Dr.	10,000	
	To A's Capital A/c $(10,000 \times \frac{5}{8})$			6,250
	To B's Capital A/c $(10,000 \times \frac{3}{8})$			3,750
	(Adjustment for C's share of workmen compensation claim of ₹1,50,000 *less* reserve ₹1,00,000 in gaining ratio of 5 : 3)			

ILLUSTRATION 65.

A, B, C and D were sharing profits in the ratio of 3 : 2 : 3 : 2. A retires and the new profit sharing ratio is agreed at 3 : 3 : 4. An extract of their Balance Sheet as at that date is:

BALANCE SHEET *as at* ....

Liabilities	₹	*Assets*	₹
Investment Fluctuation Reserve	90,000	Investments (at Cost)	5,00,000

B, C and D agreed that book value of any item of Balance Sheet is not to be altered and any adjustment is to be made by passing an adjustment entry. Show the accounting treatment under the following alternative cases :

Case (*i*) If there is no other information.
Case (*ii*) If the market value of investments is ₹5,00,000
Case (*iii*) If the market value of investments is ₹4,70,000
Case (*iv*) If the market value of investments is ₹3,80,000
Case (*v*) If the market value of investments is ₹5,20,000

SOLUTION :

Calculation of Gaining Ratios : (New Ratio – Old Ratio)

$$B = \frac{3}{10} - \frac{2}{10} = \frac{1}{10}$$

$$C = \frac{3}{10} - \frac{3}{10} = \text{Nil}$$

$$D = \frac{4}{10} - \frac{2}{10} = \frac{2}{10}$$

Thus, Gaining Ratio between B and D is 1 : 2.

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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
Case (*i*)	*B*'s Capital A/c $(27{,}000 \times \frac{1}{3})$	Dr.		9,000	
	D's Capital A/c $(27{,}000 \times \frac{2}{3})$	Dr.		18,000	
	To *A*'s Capital A/c $(90{,}000 \times \frac{3}{10})$				27,000
	(*A*'s share of investment fluctuation reserve adjusted in gaining ratio of 1 : 2)				
Case (*ii*)	Same entry as given in Case (*i*)				
Case (*iii*)	*B*'s Capital A/c $(18{,}000 \times \frac{1}{3})$	Dr.		6,000	
	D's Capital A/c $(18{,}000 \times \frac{2}{3})$	Dr.		12,000	
	To *A*'s Capital A/c $(60{,}000 \times \frac{3}{10})$				18,000
	(*A*'s share of investment fluctuation reserve of ₹90,000 *less* ₹30,000 for fall in the value of investments adjusted in gaining ratio of 1 : 2)				
Case (*iv*)	*A*'s Capital A/c $(30{,}000 \times \frac{3}{10})$	Dr.		9,000	
	To *B*'s Capital A/c $(9{,}000 \times \frac{1}{3})$				3,000
	To *D*'s Capital A/c $(9{,}000 \times \frac{2}{3})$				6,000
	(*A*'s share of fall in the value of investments ₹1,20,000 *less* reserve ₹90,000 adjusted in gaining ratio of 1 : 2)				
Case (*v*)	*B*'s Capital A/c $(33{,}000 \times \frac{1}{3})$	Dr.		11,000	
	D's Capital A/c $(33{,}000 \times \frac{2}{3})$	Dr.		22,000	
	To *A*'s Capital A/c $(1{,}10{,}000 \times \frac{3}{10})$				33,000
	(*A*'s share of investment fluctuation reserve ₹90,000 plus ₹20,000 for increase in the value of investments adjusted in gaining ratio)				

ILLUSTRATION 66.

A, *B* and *C* are partners sharing profits and losses in the ratio of 2 : 2 : 1. Their Balance Sheet as at 31st March, 2022 is as under :

Liabilities	₹	*Assets*	₹
Creditors	1,50,000	Fixed Assets	7,00,000
Profit & Loss Balance	20,000	Investments	

Reserve Fund	1,00,000	(Market Value ₹1,10,000)	1,50,000
Provident Fund	25,000	Current Assets	3,60,000
Workmen Compensation Reserve	80,000	Advertisement Suspense Account	20,000
Investment Fluctuation Reserve	30,000	Current Account : *C*	10,000
Capitals : *A* 4,00,000			
B 2,00,000			
C 2,00,000	8,00,000		
Current Accounts :			
A 20,000			
B 15,000	35,000		
	12,40,000		12,40,000

A retires on this date and *B* and *C* agreed to share future profits and losses in the ratio of 5 : 3. Claim on account of Workmen's Compensation is estimated at ₹50,000.

You are required to record the effect of retirement by a single journal entry. Also prepare the partner's current accounts.

SOLUTION :

(*i*) Adjustments to be made for :

		₹
Profit & Loss Balance		20,000
Reserve Fund		1,00,000
Workmen Compensation Reserve (₹80,000 less claim ₹50,000)		30,000
		1,50,000
Less : Investment Fluctuation Reserve (Fall in the value of Investments ₹40,000 less investment fluctuation reserve ₹30,000)	10,000	
Advertisement Suspense Account	20,000	30,000
		1,20,000

(*ii*) Gaining Ratios : (New Ratio – Old Ratio)

$$B = \frac{5}{8} - \frac{2}{5} = \frac{25-16}{40} = \frac{9}{40}$$

$$C = \frac{3}{8} - \frac{1}{5} = \frac{15-8}{40} = \frac{7}{40}$$

$$\text{Gaining Ratio} = \frac{9}{40} : \frac{7}{40} \text{ or } 9 : 7$$

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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
March 31	*B*'s Current A/c $(48{,}000 \times \frac{9}{16})$	Dr.		27,000	
	C's Current A/c $(48{,}000 \times \frac{7}{16})$	Dr.		21,000	
	To *A*'s Current A/c $(1{,}20{,}000 \times \frac{2}{5})$				48,000
	(Adjustment for accumulated profits and losses on *A*'s retirement)				

PARTNER'S CURRENT ACCOUNTS

Dr. Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
31.3.2022				*31.3.2022*			
To Bal. b/d			10,000	By Bal b/d	20,000	15,000	
To *A*'s Current A/c		27,000	21,000	By *B*'s Current A/c	27,000		
To *A*'s Capital A/c (Transfer)	68,000			By *C*'s Current A/c	21,000		
				By Bal. c/d		12,000	31,000
	68,000	27,000	31,000		68,000	27,000	31,000

ILLUSTRATION 67.

Following is the Balance Sheet of *X*, *Y* and *Z* as at 31st March 2022, who are sharing profits in the ratio of 3 : 2 : 1.

Liabilities		₹	*Assets*		₹
Capital A/cs :			Land and Buildings		6,00,000
X	3,20,000		Machinery		1,50,000
Y	2,40,000		Investments		
Z	1,20,000	6,80,000	(Market Value ₹1,75,000)		2,00,000
Profit & Loss Account		75,000	Sundry Debtors	1,50,000	
General Reserve		60,000	*Less :* Provision for		
Workmen Compensation Reserve		50,000	Doubtful		
Investment Fluctuation Reserve		40,000	Debts	6,000	1,44,000
Creditors		2,95,000	Cash at Bank		70,000
			Advertisement Expenditure		36,000
		12,00,000			12,00,000

Z retires from 1st April, 2022 and *X* and *Y* decided to share future profits in the ratio of 1 : 2. Following was agreed upon :

(*i*) Land and Building was found undervalued by ₹1,00,000 and Machinery was found overvalued by ₹37,000.

(*ii*) Provision for Doubtful Debts is to be made equal to 6% of the debtors.

(*iii*) Goodwill is to be valued at ₹1,20,000.

(*iv*) Claim on account of Workmen Compensation is ₹20,000

(*v*) *X* and *Y* decide that after adjusting Workmen Compensation Claim from Workmen Compensation Reserve and difference between Book Value and Market Value of investments from Investment Fluctuation Reserve, remaining balance of such reserves and all accumulated profits/losses are to appear in the Balance Sheet of the new firm. *Z*'s share in these accumulated profits and losses should be adjusted by opening Current Accounts of *X* and *Y*.

Pass the necessary Journal entries and prepare the Revaluation Account, Partner's Capital Accounts and the Balance Sheet.

SOLUTION :

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Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2022					
April 1	Land and Buildings A/c	Dr.		1,00,000	
	To Revaluation A/c				1,00,000
	(Increase in the value of Land and Building)				
April 1	Revaluation A/c	Dr.		40,000	
	To Machinery A/c				37,000
	To Provision for Doubtful Debts A/c				3,000
	(Decrease in the value of Machinery and increase in provision)				
April 1	Revaluation A/c	Dr.		60,000	
	To X's Capital A/c				30,000
	To Y's Capital A/c				20,000
	To Z's Capital A/c				10,000
	(Transfer of profit on revaluation)				
April 1	Y's Capital A/c ($\frac{2}{6}$ of ₹1,20,000)	Dr.		40,000	
	To X's Capital A/c ($\frac{1}{6}$ of ₹1,20,000)				20,000
	To Z's Capital A/c ($\frac{1}{6}$ of 1,20,000)				20,000
	(Adjustment for goodwill by debiting gaining partner and crediting sacrificing partners) (Working Note 1)				
April 1	Workmen Compensation Reserve A/c	Dr.		20,000	
	To Workmen Compensation Claim A/c				20,000
	(Adjustment for Workmen Compensation Claim)				
April 1	Investment Fluctuation Reserve A/c	Dr.		25,000	
	To Investments A/c				25,000
	(Adjustment for book value and market value of investments)				
April 1	Y's Current A/c ($\frac{2}{6}$ of ₹1,44,000)	Dr.		48,000	
	To X's Current A/c ($\frac{1}{6}$ of ₹1,44,000)				24,000
	To Z's Capital A/c ($\frac{1}{6}$ of ₹1,44,000)				24,000
	(Adjustment for accumulated profits/losses by debiting gaining partner and crediting sacrificing partners) (Working Note 2)				
April 1	Z's Capital A/c	Dr.		1,74,000	
	To Z's Loan A/c				1,74,000
	(Amount due to Z transferred to his Loan Account)				

REVALUATION ACCOUNT

Dr. Particulars		₹	Particulars	Cr. ₹
To Machinery A/c		37,000	By Land and Buildings A/c	1,00,000
To Provision for Doubtful Debts A/c		3,000		
To Gain on Revaluation transferred to :				
X's Capital A/c	30,000			
Y's Capital A/c	20,000			
Z's Capital A/c	10,000	60,000		
		1,00,000		1,00,000

PARTNER'S CAPITAL ACCOUNTS

Dr. Particulars	X	Y	Z	Particulars	X	Y	Cr. Z
	₹	₹	₹		₹	₹	₹
To X's Capital A/c		20,000		By Balance b/d	3,20,000	2,40,000	1,20,000
To Z's Capital A/c		20,000		By Revaluation	30,000	20,000	10,000
To Z's Loan A/c			1,74,000	By Y's Capital A/c	20,000		20,000
To Balance c/d	3,70,000	2,20,000		By Y's Current A/c			24,000
	3,70,000	2,60,000	1,74,000		3,70,000	2,60,000	1,74,000

BALANCE SHEET

as at 1st April, 2022

Liabilities		₹	Assets		₹
Capital A/cs :			Land and Buildings		7,00,000
X	3,70,000		Machinery		1,13,000
Y	2,20,000	5,90,000	Investments		1,75,000
Profit & Loss Account		75,000	Sundry Debtors	1,50,000	
General Reserve		60,000	*Less :* Provision for Doubtful Debts	9,000	1,41,000
Workmen Compensation Claim		20,000	Cash at Bank		70,000
Workmen Compensation Reserve (₹50,000 – ₹20,000)		30,000	Y's Current Account		48,000
Investment Fluctuation Reserve (₹40,000 – ₹25,000)		15,000	Advertisement Expenditure		36,000
X's Current Account		24,000			
Z's Loan Account		1,74,000			
Creditors		2,95,000			
		12,83,000			12,83,000

Working Notes :

(1) Calculation of Gaining/Sacrifice Ratio

	New Share	Old Share	
X	$\frac{1}{3}$	$\frac{3}{6}$	$\frac{1}{3}-\frac{3}{6}=\frac{1}{6}$ Sacrifice
Y	$\frac{2}{3}$	$\frac{2}{6}$	$\frac{2}{3}-\frac{2}{6}=\frac{2}{6}$ Gain
Z	—	$\frac{1}{6}$	$\frac{1}{6}$ Sacrifice

(2) Adjustment for Accumulated Profits/Losses :

	₹
Profit & Loss Account	75,000
General Reserve	60,000
Workmen Compensation Reserve (₹50,000 – ₹20,000)	30,000
Investment Fluctuation Reserve (₹40,000 – ₹25,000)	15,000
	1,80,000
Less : Advertisement Expenditure Account	36,000
Net Amount	1,44,000

ILLUSTRATION 68.

A, *B* and *C* are partners sharing profits in the ratio of $\frac{4}{9}:\frac{1}{3}:\frac{2}{9}$. *B* retires on 1st April 2017 and *A* and *C* decide to share future profits in 5 : 4. Following is their Balance Sheet as at 31st March, 2022 :

Liabilities		₹	*Assets*		₹
Creditors		1,60,000	Plant & Machinery		5,00,000
Profit & Loss Account		1,80,000	Goodwill		45,000
General Reserve		2,20,000	Investments		
Employee's Provident Fund		30,000	(Market Value ₹1,80,000)		1,50,000
Workmen Compensation Reserve		70,000	Closing Stock		2,15,000
Investment Fluctuation Reserve		20,000	Sundry Debtors	2,00,000	
Capital A/cs :			*Less :* Provision for		
A	2,80,000		Doubtful		
B	2,40,000		Debts	5,000	1,95,000
C	2,00,000	7,20,000	Cash at Bank		2,43,000
			Advertisement Suspense		52,000
		14,00,000			14,00,000

Following adjustments were agreed upon :

(*i*) Goodwill of the firm is valued at ₹1,35,000.

(*ii*) Plant & Machinery is to be depreciated to ₹4,45,000.

(*iii*) A computer previously written off is sold for ₹8,000.

(*iv*) A liability of claim included in creditors for ₹20,000 is settled at ₹15,000.

(*v*) There were bad debts ₹20,000.

(*vi*) The claim on account of Workmen Compensation Reserve is determined at ₹24,000.

(*vii*) *A* and *C* decided that general reserves and accumulated profits/losses are to appear in the books of the new firm at their original figures after adjusting claim of Workmen Compensation from Workmen Compensation Reserve.

(*viii*) Capital of the new firm in total will be the same as before retirement of *B* and will be in the new profit sharing ratio of the continuing partners.

(*ix*) 50% is to be paid to *B* immediately and balance in two equal instalments together with interest @ 8% p.a.

Prepare Revaluation Account, Capital Accounts and Balance Sheet of the firm after *B*'s retirement.

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Plant & Machinery A/c	55,000	By Bank (Computer sold)		8,000
To Bad Debts (Note 1)	15,000	By Creditors A/c		5,000
		By Investments A/c		30,000
		By Loss transferred to :		
		A's Capital A/c	12,000	
		B's Capital A/c	9,000	
		C's Capital A/c	6,000	27,000
	70,000			70,000

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Goodwill A/c	20,000	15,000	10,000	By Balance b/d	2,80,000	2,40,000	2,00,000
To Revaluation A/c	12,000	9,000	6,000	By *A*'s Capital A/c		15,000	
To *B*'s Capital A/c	15,000		30,000	By *C*'s Capital A/c		30,000	
To *B*'s Capital A/c	46,000		92,000	By *A*'s Capital A/c		46,000	
To Balance c/d	1,87,000	3,99,000	62,000	By *C*'s Capital A/c		92,000	
	2,80,000	4,23,000	2,00,000		2,80,000	4,23,000	2,00,000
To Bank A/c		1,99,500		By Balance b/d	1,87,000	3,99,000	62,000
To *B*'s Loan A/c		1,99,500		By Bank A/c (Bal. figure)	2,13,000		2,58,000
To Balance c/d (Note 5)	4,00,000		3,20,000				
	4,00,000	3,99,000	3,20,000		4,00,000	3,99,000	3,20,000

BALANCE SHEET
as at 1st April, 2022

Liabilities		₹	*Assets*	₹
Creditors		1,40,000	Plant & Machinery	4,45,000
Profit & Loss Account		1,80,000	Investments	1,80,000
General Reserve		2,20,000	Closing Stock	2,15,000
Employee's Provident Fund		30,000	Sundry Debtors	1,80,000
Workmen Compensation Claim		24,000	Cash at Bank (Note 4)	5,07,500
Workmen Compensation Reserve (₹70,000 – ₹24,000)		46,000	Advertisement Suspense	52,000
Investment Fluctuation Reserve		20,000		
Capital A/cs :				
A	4,00,000			
C	3,20,000	7,20,000		
B's Loan Account		1,99,500		
		15,79,500		15,79,500

Working Notes :

(1) Entries for Bad Debts

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	Bad Debts A/c	Dr.		20,000	
	To Sundry Debtors A/c				20,000
	Provision for Doubtful Debts A/c	Dr.		5,000	
	Revaluation A/c	Dr.		15,000	
	To Bad Debts A/c				20,000

(2) Calculation of Gain/Sacrifice Ratio :

	A	*B*	*C*
New Share	$\frac{5}{9}$	—	$\frac{4}{9}$
Old Share	$\frac{4}{9}$	$\frac{1}{3}$ or $\frac{3}{9}$	$\frac{2}{9}$
	$\frac{1}{9}$ Gain	$\frac{3}{9}$ Sacrifice	$\frac{2}{9}$ Gain

Gaining Ratio between *A* and *C* = 1 : 2

Entry for Goodwill :

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	A's Capital A/c ($\frac{1}{3}$ of ₹45,000)	Dr.		15,000	
	C's Capital A/c ($\frac{2}{3}$ of ₹45,000)	Dr.		30,000	
	To *B*'s Capital A/c ($\frac{3}{9}$ of ₹1,35,000)				45,000

(3) Calculation of Net Effect of Accumulated Profits/Losses :

	₹
Profit and Loss A/c (Cr.)	1,80,000
General Reserve	2,20,000
Workmen Compensation Reserve (₹70,000 – ₹24,000)	46,000
Investment Fluctuation Reserve	20,000
	4,66,000
Less : Advertisement Suspense Account	52,000
Net Amount	4,14,000

Adjustment Entry :

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	A's Capital A/c ($\frac{1}{3}$ of ₹1,38,000)	Dr.		46,000	
	C's Capital A/c ($\frac{2}{3}$ of ₹1,38,000)	Dr.		92,000	
	To *B*'s Capital A/c ($\frac{3}{9}$ of ₹4,14,000)				1,38,000

(4) BANK ACCOUNT

Particulars	₹	Particulars	₹
To Balance b/d	2,43,000	By Creditors	15,000
To Revaluation (Computer Sold)	8,000	By *B*'s Capital A/c	1,99,500
To *A*'s Capital A/c	2,13,000	By Balance c/d	5,07,500
To *C*'s Capital A/c	2,58,000		
	7,22,000		7,22,000

(5) Adjustment of Capitals :

		₹
Total Capital of new firm	= Opening Capitals of *A*, *B* and *C*	7,20,000
A's Capital in the new firm	$= \frac{5}{9}$ of ₹7,20,000 =	4,00,000
C's Capital in the new firm	$= \frac{4}{9}$ of ₹7,20,000 =	3,20,000

ILLUSTRATION 69.

X, *Y* and *Z* are partners sharing profits in the ratio of 4 : 3 : 2. Following is their Balance Sheet as at 31st December, 2021 :

Liabilities		₹	Assets		₹
Sundry Creditors		71,000	Cash at Bank		1,58,000
Profit & Loss Account		40,000	Sundry Debtors	3,20,000	
General Reserve		1,05,000	*Less :* Provision for Doubtful Debts	20,000	3,00,000
Workmen Compensation Reserve		84,000	Closing Stock		1,40,000
Capital A/cs :			Office Equipments		70,000
X	5,00,000		Investments (Market Value ₹1,00,000)		1,10,000
Y	4,00,000		Land and Building		6,00,000
Z	2,00,000	11,00,000			

		Advertisement Suspense Account	22,000
	14,00,000		14,00,000

Y retires on 1st January, 2022 and *X* and *Z* decided to share future profits and losses in the ratio of 5 : 3.

It was agreed that :

(*i*) A Computer purchased on 1st April, 2021 for ₹40,000 debited to Office Expenses Account is to be brought into account charging depreciation @ 10% p.a.

(*ii*) Accrued income of ₹1,000 is to be provided for.

(*iii*) A sum of ₹15,000 is to be written off from Debtors.

(*iv*) Closing Stock is to be written down to ₹1,20,000 and Land and Building is to be written up by ₹1,00,000.

(*v*) General Reserve is to appear in the books at ₹60,000.

(*vi*) Since there was no claim against Workmen Compensation Reserve, it was agreed that it should appear in the books at ₹30,000.

(*vii*) Balance of Profit & Loss Account and Advertisement Suspense Account is to be carried forward in the new firm's Balance Sheet.

(*viii*) 20% of the amount payable to *Y* was paid in cash and balance was transferred to his Loan Account.

Prepare Revaluation Account, Partner's Capital Accounts and the new Balance Sheet of the firm.

SOLUTION :

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Closing Stock		20,000	By Office Equipments A/c(1)	37,000
To Investments		10,000	By Accrued Income	1,000
To Gain transferred to :			By Land & Building	1,00,000
X's Capital A/c	48,000			
Y's Capital A/c	36,000			
Z's Capital A/c	24,000	1,08,000		
		1,38,000		1,38,000

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*X*	*Y*	*Z*	*Particulars*	*X*	*Y*	*Z*
	₹	₹	₹		₹	₹	₹
To *Y*'s Capital A/c(3)	19,500		16,500	By Balance b/d	5,00,000	4,00,000	2,00,000
To Bank A/c (20% of ₹5,05,000)		1,01,000		By Revaluation A/c	48,000	36,000	24,000
To *Y*'s Loan A/c		4,04,000		By Gen. Res. A/c	20,000	15,000	10,000
To Balance c/d	5,72,500		2,29,500	By Workmen Compensation Res.	24,000	18,000	12,000

				By X's Capital A/c		19,500	
				By Z's Capital A/c		16,500	
	5,92,000	5,05,000	2,46,000		5,92,000	5,05,000	2,46,000

BALANCE SHEET *as at 1st Jan., 2022*

Liabilities		₹	*Assets*		₹
Sundry Creditors		71,000	Cash at Bank		
Profit & Loss Account		40,000	(₹1,58,000 – ₹1,01,000)		57,000
General Reserve		60,000	Accrued Income		1,000
Workmen Compensation Reserve		30,000	Sundry Debtors	3,05,000	
Y's Loan Account		4,04,000	*Less :* Provision for Doubtul Debts	5,000	3,00,000
Capital Accounts :					
X	5,72,500				
Z	2,29,500	8,02,000	Closing Stock		1,20,000
			Office Equipments (₹70,000 + ₹37,000)		1,07,000
			Investments		1,00,000
			Land and Building		7,00,000
			Advertisement Suspense Account		22,000
		14,07,000			14,07,000

Working Notes :

(1)

	₹
Computer purchased on 1st April, 2021	40,000
Less : Depreciation @ 10% p.a. for nine months	3,000
Value of Computer on 31st Dec., 2021 :	37,000

(2) Entries for Bad Debts :

Bad Debts A/c	Dr.	15,000	
To Sundry Debtors A/c			15,000
Provision for Doubtful Debts A/c	Dr.	15,000	
To Bad Debts A/c			15,000

(3) Gaining Ratio of Partners :

$$X \quad \frac{5}{8}-\frac{4}{9}=\frac{45-32}{72}=\frac{13}{72}$$

$$Z \quad \frac{3}{8}-\frac{2}{9}=\frac{27-16}{72}=\frac{11}{72}$$

Adjustment of Accunulated Profits/Losses :	₹
Profit & Loss Account	40,000
General Reserve	60,000
Workmen Compenstion Reserve	30,000
	1,30,000
Less : Advertisement Suspense Account	22,000
Net amount	1,08,000

Adjustment Journal Entry :

X's Capital A/c ($\frac{13}{24}$ of 36,000)	Dr.	19,500	
Z's Capital A/c ($\frac{11}{24}$ of 36,000)	Dr.	16,500	
To Y's Capital A/c ($\frac{3}{9}$ of 1,08,000)			36,000

ILLUSTRATION 70.

Vimal, Sanjay and Rusha are partners in a firm sharing profits and losses in proportion to their capitals. Their Balance Sheet as at 31st March, 2017, is given below:

Liabilities		₹	*Assets*		₹
Sundry Creditors		10,000	Cash at Bank		5,000
Workmen Compensation Reserve		3,000	Sundry Debtors	22,000	
Employee's Provident Fund		7,000	*Less :* Prov. for		
Capital Accounts :			Doubtful Debts	2,000	20,000
Vimal	40,000		Stock		20,000
Sanjay	30,000		Plant & Machinery		30,000
Rusha	30,000	1,00,000	Land & Building		40,000
			Advertisement Expenditure		5,000
		1,20,000			1,20,000

Sanjay retired on 1st April, 2017, on the following terms :

(*a*) Land & Building to be appreciated by 30%.

(*b*) Plant & Machinery to be depreciated to 70%.

(*c*) Bad debts ₹3,000 to be written off.

(*d*) The claim, on account of Workmen Compensation Fund, was estimated at ₹2,000.

(*e*) Sanjay to be paid ₹45,000 for which sufficient loan be taken from the bank.

(*f*) Vimal and Rusha, in the new firm, to share profits and losses in the ratio of 3 : 2.

(*g*) It was decided that the advertisement expenditure would be carried forward in the new firm's balance sheet.

You are required to :

(*i*) Pass journal entries on the date of Sanjay's retirement.

(*ii*) Prepare the Opening Balance Sheet of the new firm on the completion of the transactions. (Show your workings clearly).

(I.S.C. Specimen Question Paper, 2018)

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2017 April 1	Land & Building A/c	Dr.		12,000	
	To Revaluation A/c				12,000
	(Increase in the value of Land & Building)				
April 1	Revaluation A/c	Dr.		9,000	
	To Plant & Machinery				9,000
	(Decrease in the value of Plant & Machinery)				
April 1	Bad Debts A/c	Dr.		3,000	
	To Sundry Debtors A/c				3,000
	(Bad Debts written off)				
April 1	Provision for Doubtful Debts A/c	Dr.		2,000	
	Revaluation A/c	Dr.		1,000	
	To Bad Debts A/c				3,000
	(Bad Debts adjusted against provision)				
April 1	Revaluation A/c	Dr.		2,000	
	To Vimal's Capital A/c				800
	To Sanjay's Capital A/c				600
	To Rusha's Capital A/c				600
	(Transfer of profit on revaluation)				
April 1	Workmen Compensation Reserve A/c	Dr.		3,000	
	To Provision for Workmen Compensation Claim A/c				2,000
	To Vimal's Capital A/c				400
	To Sanjay's Capital A/c				300
	To Rusha's Capital A/c				300
	(Surplus Workmen Compensation reserve credited to partner's Capital Accounts)				
April 1	Sanjay's Capital A/c ($\frac{3}{10}$ of 5,000)[1]	Dr.		1,500	
	To Vimal's Capital A/c ($\frac{2}{3}$ of ₹1,500)				1,000
	To Rusha's Capital A/c ($\frac{1}{3}$ of ₹1,500)				500
	(Adjustment for advertisement expenditure in gaining ratio of 2 : 1)				
April 1	Bank A/c	Dr.		40,000	
	To Bank Loan A/c				40,000
	(Loan taken from bank)				
April 1	Vimal's Capital A/c	Dr.		10,400	
	Rusha's Capital A/c	Dr.		5,200	
	To Sanjay's Capital A/c[2]				15,600
	(Sanjay's share of goodwill adjusted in gaining ratio of 2 : 1)				

April 1	Sanjay's Capital A/c To Bank A/c (Payment made to Sanjay)	Dr.	45,000	45,000

BALANCE SHEET
as at 1st April, 2017

Liabilities		₹	*Assets*	₹
Sundry Creditors		10,000	Sundry Debtors (₹22,000 – ₹3,000)	19,000
Provision for Workmen Compensation Claim		2,000	Stock	20,000
Employee's Provident Fund		7,000	Plant & Machinery	21,000
Bank Loan		40,000	Land & Building	52,000
Capital Accounts :			Advertisement Expenditure	5,000
Vimal	31,800			
Rusha	26,200	58,000		
		1,17,000		1,17,000

Working Notes :

(1) Old Profit Sharing Ratio of Vimal, Sanjay and Rusha = 4 : 3 : 3

New Profit Sharing Ratio of Vimal and Rusha = 3 : 2

Gaining Ratio : Vimal : $\frac{3}{5} - \frac{4}{10} = \frac{6-4}{10} = \frac{2}{10}$

Rusha : $\frac{2}{5} - \frac{3}{10} = \frac{4-3}{10} = \frac{1}{10}$

Advertisement Expenditure of ₹5,000 will be adjusted in the Gaining Ratio of 2 : 1.

(2)

		₹
Amount agreed to be paid to Sanjay		45,000
Less :	Sanjay's Capital (after all adjustments) (₹30,000 + Revaluation Profit 600 + Workmen Compensation Res. 300 – Advertisement Exp. ₹1,500)	29,400
His share of Hidden Goodwill		15,600

Sanjay's share of Goodwill has been debited to Vimal and Rusha in their gaining ratio of 2 : 1.

(3)

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*Vimal*	*Sanjay*	*Rusha*	*Particulars*	*Vimal*	*Sanjay*	*Rusha*
	₹	₹	₹		₹	₹	₹
To Vimal's Capital A/c		1,000		By Balance b/d	40,000	30,000	30,000
To Rusha's Capital A/c		500		By Revaluation	800	600	600
To Sanjay's Capital A/c	10,400		5,200	By Workmen Compensation Reserve	400	300	300
To Bank A/c		45,000		By Sanjay's Capital A/c	1,000		500

To Balance c/d	31,800		26,200	By Vimal's Capital A/c		10,400	
				By Rusha's Capital A/c		5,200	
	42,200	46,500	31,400		42,200	46,500	31,400

ILLUSTRATION 71.

Manoj, Hari and Karan are partners in a firm sharing profits and losses in the ratio 4 : 2 : 1. Their Balance Sheet as at 31st March, 2019, was as follows :

BALANCE SHEET OF MANOJ, HARI AND KARAN

as at 31st March, 2019

Liabilities		₹	*Assets*	₹
Sundry Creditors		32,600	Plant and Machinery	20,000
Bills Payable		4,000	Goodwill	7,000
General Reserve		8,400	Stock	38,000
Capital Accounts :			Bank	20,000
Manoj	16,000			
Hari	14,000			
Karan	10,000	40,000		
		85,000		85,000

Hari retired from the business on 1st April, 2019. The remaining partners decided to carry on the business. The terms of retirement provided the following :

(*a*) Out of the total insurance premium paid, ₹7,000 to be treated as prepaid insurance. The amount was earlier debited to Profit & Loss Account.

(*b*) General Reserve not to be distributed.

(*c*) Hari to be paid ₹24,400 in full settlement.

You are required to prepare Partner's Capital Accounts. (*I.S.C. 2020*)

SOLUTION :

Dr. PARTNER'S CAPITAL ACCOUNTS. Cr.

Particulars	*Manoj*	*Hari*	*Karan*	*Particulars*	*Manoj*	*Hari*	*Karan*
To Goodwill A/c	4,000	2,000	1,000	By Balance b/d	16,000	14,000	10,000
To Hari's Capital A/c	1,920		480	By Revaluation	4,000	2,000	1,000
To Balance c/d	14,080	16,400	9,520	By Manoj's Capital A/c		1,920	
				By Karan's Capital A/c		480	
	20,000	18,400	11,000		20,000	18,400	11,000
To Bank		24,400		By Balance b/d	14,080	16,400	9,520
To Hari's Capital A/c	6,400		1,600	By Manoj's Capital A/c			

To Balance c/d	7,680		7,920	(4/5 of 8,000)		6,400	
				By Karan's Capital A/c (1/5 of 8,000)		1,600	
	14,080	24,400	9,520		14,080	24,400	9,520

Working Notes :

(1) Hari's share of General Reserve : $8{,}400 \times \frac{2}{7} = 2{,}400$

Manoj's Capital A/c ($\frac{4}{5}$ of 2,400)	Dr.	1,920	
Karan's Capital A/c ($\frac{1}{5}$ of 2,400)	Dr.	480	
To Hari's Capital A/c			2,400

(2)

		₹
Hari's Capital after all adjustments :		16,400
Amount agreed to be paid in full settlement		24,400
Hari's share of Hidden Goodwill		8,000

Manoj's Capital A/c ($\frac{4}{5}$ of 8,000)	Dr.	6,400	
Karan's Capital A/c ($\frac{1}{5}$ of 8,000)	Dr.	1,600	
To Hari's Capital A/c			8,000

SHORT ANSWER QUESTIONS

1. How will you deal Goodwill at the time of retirement of a partner?

2. What are the adjustments required on retirement of a partner from the firm?

3. What is gaining ratio? How is it calculated at the time of the retirement of a partner?

4. Give two circumstances in which Gaining Ratio may be applied.

Ans. Gaining Ratio may be applied in the following circumstances :

(*i*) When there is a change in profit-sharing ratio.

(*ii*) When a partner retires/dies, for adjustment of his share of goodwill.

5. How goodwill is recorded on the retirement or death of a partner?

Ans. Remaining Partner's Capital A/cs Dr. (In Gaining Ratio)
To Retiring or Deceased Partner's Capital A/c (with his share of goodwill)

6. *P*, *Q* and *R* share profits in the ratio of 5 : 4 : 3. *R* retires and the new ratio is 5 : 3. If *R* is given ₹60,000 as goodwill, what will be the journal entry?

Ans. *P*'s Capital A/c	Dr.	50,000	
Q's Capital A/c	Dr.	10,000	
To *R*'s Capital A/c			60,000

7. State the purpose for which 'sacrificing' and 'gaining ratios' are calculated.

Ans. The purpose of calculating sacrificing ratio is, that, on the admission of a new partner, incoming partner's share of goodwill is credited to the old partners in the ratio in which they have sacrificed their share in favour of the new partner. On the retirement or death of a partner, the retiring or deceased partner's share of goodwill is credited to his Capital Account and debited to the continuing partner's Capital Accounts in their gaining ratio.

8. Distinguish between sacrificing ratio and gaining ratio in the context of partnership accounting without giving an example. *(I.S.C. 2005)*

9. State the ratio in which profit or loss on revaluation will be shared by the partners when a partner retires.

Ans. In case of retirement, any profit or loss on revaluation of assets and liabilities will be shared by all the partners (including the retiring partner) in their old profit sharing ratio.

10. Why are assets and liabilities revalued at the time of retirement of a partner?

Ans. At the time of retirement assets and liabilities are revalued because with the passage of time the value of certain assets might have increased whereas the value of certain other assets might have decreased. Thus, the realisable value of various assets and the actual position of liabilities may be different from the values stated in the balance sheet. It is, therefore, necessary that all the assets and liabilities of the firm are brought to their true values on the date of retirement of a partner so that neither the retiring partner nor the continuing partners are put to any disadvantage.

11. How are accumulated profits and losses dealt with when a partner retires from a firm?

Ans. At the time of retirement all accumulated profits (such as General Reserve, Credit balance of Profit & Loss Account etc.) should be credited to all partner's Capital Accounts (including the retiring partner) and all accumulated losses (such as Debit balance of Profit & Loss Account) should be debited to all partner's Capital Accounts (including the retiring partner) in their old profit sharing ratio. The reason is that all such profits and losses arose when the retiring partner was also a partner in the firm.

12. How would you calculate the amount payable to the representative of a deceased partner?

13. If a partner dies during the year, how will you find out the share of profit of the deceased partner?

14. Name five items which are credited to the account of the representatives of the deceased partner.

15. What is the entitlement of the legal representative of a deceased partner in the subsequent profits of the firm? *(I.S.C. 2001)*

Ans. As per section 37 of the Partnership Act, the deceased partner's executor's would be entitled, at their discretion, to interest at 6% p.a. on the amount due from the date of death to the date of actual payment or to that portion of profit which is earned by the firm with the help of the amount due to the deceased partner. This also applies to a retiring partner.

16. Name four items which are credited to the account of a deceased partner while calculating the amount due to his legal representatives. *(I.S.C. 2006)*

Ans. (*i*) The amount standing to the credit of his Capital Account.

(*ii*) His share in the goodwill of the firm.

(*iii*) His share of profit on the revaluation of assets and liabilities.

(*iv*) His share of the undistributed profits and reserves.

17. What is gaining ratio? *(I.S.C. 2007)*

Ans. Gaining ratio is the ratio in which the retired or deceased partner's share is acquired by the continuing partners. The retiring or deceased partner's capital account will be credited with his share of goodwill and continuing partner's capital accounts will be debited in their gaining ratio.

18. When is a partner liable for debts incurred by the firm after his retirement? *(I.S.C. 2007)*

Ans. A retiring partner continues to be liable for debts incurred by the firm after his retirement until public notice of his retirement is given by himself or any of the other partners. However, he will not be liable to any third party if the latter deals with the firm without knowing that the former was a partner. [Sec 32 (3) & (4)]

19. Give two differences between Sacrificing Ratio and Gaining Ratio. *(I.S.C. 2012)*

20. Give the Journal entry to distribute 'Workmen Compensation Reserve' of ₹70,000 at the time of retirement of Neeti when there is a claim of ₹25,000 against it. The firm has three partners Raveena, Neeti and Rajat.

Ans.

Workmen Compensation Reserve A/c	Dr.	70,000	
To Liability for Workmen Compensation Claim A/c			25,000
To Raveena's Capital A/c			15,000
To Neeti's Capital A/c			15,000
To Rajat's Capital A/c			15,000
(Transfer of Workmen Compensation Reserve)			

21. How will the firm show the amount payable to the retiring partner, if it is not in a position to immediately pay the amount due to him on his retirement? *(I.S.C. 2013)*

Ans. By transferring the amount due to him, to his Loan Account which will then be shown on the liabilities side of the Balance Sheet of the reconstituted firm.

22. List any four items that may have to be deducted from a deceased partner's capital account while computing the amount payable to his legal representatives. *(I.S.C. 2014)*

Ans. (*i*) Drawings

(*ii*) Interest on Drawings

(*iii*) His share of loss on revaluation of the assets and reassessment of liabilities.

(*iv*) His share of undistributed loss, such as debit balance of Profit and Loss Account.

23. Give the formula for calculating the outgoing partner's share in the interim profits of the firm, on the basis of sales made by the firm. (I.S.C. 2016)

Ans. Outgoing partner's share in profit till the date of retirement or death shall be :

Sales from the date of last B/S $\times \frac{\text{Previous year's Profit}}{\text{Previous year's Sales}} \times$ Retiring or Deceased Partner's share of profit

24. Give the journal entry for closing the retiring partner's capital account when his share is paid to him privately by the remaining partners. (I.S.C. 2019)

Ans. Retiring Partner's Capital A/c Dr.
To Remaining/Continuing Partners Capital A/cs

OBJECTIVE TYPE QUESTIONS

Fill in the blanks :

(*i*) *A, B* and *C* are partners sharing profits in the ratio of $\frac{1}{2} : \frac{1}{4} : \frac{1}{4}$. On the retirement of *B*, the new ratio will be ....

(*ii*) *A, B* and *C* are partners sharing profits in the ratio of $\frac{1}{4} : \frac{3}{10} : \frac{9}{20}$. On the retirement of *C*, the new ratio will be ....

(*iii*) *A, B* and *C* are partners sharing profits in the ratio of 5 : 2 : 1. If the new ratio on the retirement of *C* is 5 : 2, gaining ratio will be ....

(*iv*) *P, Q* and *R* are partners sharing profits in the ratio of 5 : 4 : 3. *Q* retires and *P* and *R* decide to share future profits equally. The gaining ratio will be ....

(*v*) *P, Q* and *R* share profits in the ratio of 5 : 4 : 3. *R* retires and the new ratio is 5 : 3. If *R* is given ₹6,000 as goodwill, *P* and *Q* will be debited from ₹............... and ₹............... respectively.

Ans. (*i*) 2 : 1; (*ii*) 5 : 6; (*iii*) 5 : 2; (*iv*) 1 : 3 (*v*) ₹5,000, ₹1,000.

PRACTICAL QUESTIONS

(Q. No. 1 to 68 are strictly in the serial order of Illustrations)

Q. 1. *A, B* and *C* are partners sharing profits in the ratio of 6 : 5 : 4. Calculate new profit sharing ratios if *(i) A* retires; *(ii) B* retires; *(iii) C* retires.

[**Ans.** (*i*) 5 : 4; (*ii*) 6 : 4; (*iii*) 6 : 5]

Q. 2. *X, Y* and *Z* are partners sharing profits in the ratio of 2/3 : 1/4 : 1/12. Calculate the new ratio if *X* retires.

[**Ans.** 3 : 1]

Q. 3. *L, M* and *O* were partners in a firm sharing profits in the ratio of 3 : 2 : 2. *M* retired and his share was divided equally between *L* and *O*. Calculate the new profit sharing ratio of *L* and *O*.

[**Ans.** 4 : 3]

Q. 4 (A). *A, B* and *C* are partners sharing profits in the ratio of 4 : 3 : 2. *B* retires and his share was taken up by *A* and *C* in the ratio of 3 : 2. Find out the new ratio.

[**Ans.** 29 : 16]

Q. 4 (B). *A, B* and *C* are partners sharing profits in the ratio of 4 : 3 : 1. *A* retires and his share is taken over by *B* and *C* equally. Calculate the new ratio.

[**Ans.** 5 : 3]

Q. 4 (C). *A, B* and *C* are partners sharing profits in the ratio of 1/2 : 1/3 : 1/6. *B* retires and his share is taken by *A* and *C* in the ratio of 5 : 3. Calculate the new ratio.

[**Ans.** 17 : 7]

Q. 4 (D). *X, Y* and *Z* are partners sharing in the ratio of 2 : 2 : 1. *Y* retires and his share is entirely taken by *Z*. Calculate the new ratio.

[**Ans.** 2 : 3]

Q. 5. *P, Q* and *R* are in partnership sharing profits and losses as 1/2, 2/6 and 1/6 respectively. *R* retires and his share is taken by *P* and *Q* in the ratio of 2 : 1. Immediately, *S* is admitted for 1/4th share of profit, 1/3rd of which was given by *P* and the remaining share was taken equally from *P* and *Q*. Calculate new profit-sharing ratio after *S*'s admission.

[**Ans.** New Profit Sharing Ratio of *P, Q* and *S* = 16 : 11 : 9.]

Q. 6. *A, B* and *C* were partners sharing profits in the ratio of 7 : 5 : 3. Find out the gaining ratio and new ratios when (*i*) *A* retires, (*ii*) *B* retires or (*iii*) *C* retires.

[**Ans.** Gaining Ratios — (*i*) 5 : 3; (*ii*) 7 : 3; (*iii*) 7 : 5,
New Ratios — (*i*) 5 : 3; (*ii*) 7 : 3; (*iii*) 7 : 5]

Q. 7 (A). On 1st April, 2022 Ashish, Namish and Aman were partners sharing profits and losses in the ratio of 2/5, 2/5 and 1/5 respectively. On this date Namish retires. The new profit sharing ratio of Ashish and Aman will be 3/4 and 1/4 respectively. Calculate gaining ratio.

[**Ans.** 7 : 1.]

Q. 7 (B). On 1st April, 2022 *A, B* and *C* were partners sharing profits and losses in the ratio of *A* 5/10, *B* 3/10 and *C* 2/10 respectively. On this date *B* retires. The new profit sharing ratio of *A* and *C* will be *A* 3/5 and *C* 2/5. Calculate gaining ratio.

[**Ans.** 1 : 2]

Q. 7 (C). *A, B* and *C* are partners sharing profits in the ratio of 1/2 : 1/3 : 1/6. *C* retires and *A* and *B* decide to share future profits equally. Calculate the gaining ratio.

[**Ans.** *A* gains nothing; *B* gains 1/6.]

Q. 7 (D). *A, B, C* and *D* are partners sharing profits in the ratio of 5 : 4 : 3 : 2. *A* retires and *B, C* and *D* decide to share the profits and losses equally in future. Calculate the gaining ratio.

[**Ans.** Gaining Ratio 2 : 5 : 8]

Q. 8. *L, M* and *N* are three partners sharing profits in the ratio of 4 : 3 : 2 respectively. *M* retires and the goodwill is valued at ₹1,08,000. No goodwill account appears as yet in the books of the firm. *L* and *N* will share profits in future in the ratio of 5 : 3 respectively. Pass Journal Entry for goodwill.

[**Ans.** *M*'s share of goodwill will be adjusted to the Capital A/cs of *L* and *N* in their Gaining Ratio 13 : 11.]

Q. 9. *A*, *B* and *C* are sharing profits in the ratio of 4 : 3 : 2. Goodwill is appearing in the books at a value of ₹42,000. *C* retires and on the day of *C*'s retirement Goodwill is valued at ₹63,000. Pass the necessary journal entries.

[**Ans.** (*i*) Goodwill of ₹42,000 will be written off in 4 : 3 : 2; (*ii*) *C*'s share of Goodwill of ₹63,000 *i.e.* ₹14,000 will be adjusted into the Capital A/cs of *A* and *B* in gaining ratio of 4 : 3.]

Q. 10. *A*, *B*, *C* and *D* are partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1 : 1. *A* and *C* decided to retire from the firm. The goodwill of the firm was valued at ₹90,000. *B* and *D* decided to share future profits in the ratio of 5 : 3.

Pass necessary journal entry for the treatment of goodwill.

[**Ans.** Debit *B* by ₹26,250 and *D* by ₹18,750; and Credit *A* by ₹30,000 and *C* by ₹15,000.]

Q. 11. Surender, Ramesh, Naresh and Mohan are partners in a firm sharing profits in 2 : 1 : 2 : 1 ratio. On the retirement of Naresh, the Goodwill was valued at ₹72,000. Surender, Ramesh and Mohan decided to share future profits equally. Pass the necessary journal entry for the treatment of goodwill.

[**Ans.**	Ramesh's Capital A/c	Dr.	12,000	
	Mohan's Capital A/c	Dr.	12,000	
	To Naresh's Capital A/c			24,000
	(Naresh share of goodwill adjusted to the accounts of continuing partners in their gaining ratio 0 : 1 : 1)]			

Q. 12. *A*, *B*, *C* and *D* are partners sharing profits in the ratio of 4 : 3 : 2 : 1. On the retirement of *B*, Goodwill was valued at ₹3,00,000. *A*, *C* and *D* decide to continue the firm sharing profits equally. Pass entries.

[**Ans.**

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
	C's Capital A/c	Dr.		40,000	
	D's Capital A/c	Dr.		70,000	
	To *A*'s Capital A/c				20,000
	To *B*'s Capital A/c				90,000]

Q. 13. *X*, *Y* and *Z* are partners sharing profits and losses in the ratio of 3 : 2 : 1. *Y* retires selling his share to *X* and *Z* for ₹1,60,000, ₹1,00,000 being paid by *X* and ₹60,000 by *Z*. The profit for the year after *Y*'s retirement is ₹2,40,000.

Pass entries to (*a*) record the sale of *Y*'s share to *X* and *Z*, and (*b*) distribute the profit between *X* and *Z*.

[**Ans.** New profit sharing ratio 17 : 7.]

Q. 14. *A*, *B*, *C* and *D* are partners sharing profits in the ratio of 4 : 3 : 2 : 2. *C* retires and the remaining partners decided to share future profits in 5 : 3 : 2. On the date of *C*'s retirement there was a debit balance of ₹30,800 in the profit and loss account. Show the necessary journal entry for the treatment of profit and loss account balance.

[**Ans.** Capital accounts of all partners will be debited in old ratio.]

Q. 15. *A*, *B* and *C* are partners sharing profits and losses in the ratio of 2 : 2 : 1. *A* retires and the new ratio between *B* and *C* is agreed at 3 : 2. Give journal entries on *A*'s retirement in the following case :

Investment Fluctuation Reserve appears in the books at ₹40,000, when Investments (market value ₹1,00,000) appear at ₹85,000.

[**Ans.**
(*i*) Investment Fluctuation Reserve of ₹40,000 will be credited to *A*, *B* and *C* in 2 : 2 : 1.
(*ii*) Debit Investments and Credit Revaluation A/c by ₹15,000.
(*iii*) Revaluation Profit of ₹15,000 will be credited to *A*, *B* and *C* in 2 : 2 : 1.

Revaluation of Assets and Liabilities

Q. 16 (A). *X*, *Y* and *Z* are partners in a firm sharing profits and losses equally. The balance sheet of the firm as at 31st March, 2020 stood as follows :

Liabilities		₹	*Assets*	₹
Creditors		1,09,000	Cash in Hand and Cash at Bank	86,000
General Reserve		60,000	Debtors	2,00,000
Provident Fund		20,000	Stock	1,00,000
Capitals :			Investments (at cost)	50,000
X	3,00,000		Freehold Property	4,00,000
Y	2,00,000		Trade Marks	20,000
Z	2,00,000	7,00,000	Goodwill	33,000
		8,89,000		8,89,000

Z retires on 1st April, 2020 subject to the following adjustments :
(*i*) Freehold Property be valued at ₹5,80,000.
(*ii*) Investments be valued at ₹47,000; and stocks be valued at ₹94,000;
(*iii*) A provision of 5% be made for doubtful debts.
(*iv*) Trade Marks are valueless.
(*v*) An item of ₹12,000 included in creditors is not likely to be claimed.
(*vi*) Goodwill be valued at one year's purchase of the average profit of the past three years. Profits ending 31st March were 2018 ₹1,20,000; 2019 ₹1,00,000 and 2020 ₹95,000.

Pass journal entries, give capital accounts and the balance sheet of the remaining partners.

[**Ans.** Profit on Revaluation ₹1,53,000; *Z*'s Loan A/c ₹2,95,000; Capitals *X* ₹3,42,500; *Y* ₹2,42,500; B/S total ₹9,97,000.]

Hints : (*i*) Goodwill appearing in the assets at ₹33,000 written off among all partners in old ratio.
(*ii*) *Z*'s share of goodwill ₹35,000 debited to *X* and *Y* in gaining ratio *i.e.*, equally.

Q. 16 (B). The Balance Sheet of *A*, *B* and *C* who were sharing profits in proportion to their Capitals stood as follows as at 1st April, 2020 :

Liabilities		₹	Assets		₹
Sundry Creditors		20,000	Bank Balance		16,000
Outstanding Expenses		2,000	Sundry Debtors	15,000	
Profit & Loss A/c		15,000	*Less* : Provision	1,000	14,000
Capitals :			Stock		35,000
A		45,000	Investments		12,000
B		30,000	Fixed Assets		50,000
C		15,000			
		1,27,000			1,27,000

C retires on the above date on the following conditions :

I. Fixed Assets be reduced by 10%.

II. Investments are revalued at ₹10,000.

III. Debtors were all good.

IV. Outstanding expenses be increased by ₹600.

V. Interest accrued on Investments ₹1,800.

VI. Goodwill of the firm be valued at ₹9,000.

Prepare capital accounts and the revised balance sheet.

[**Ans.** Loss on Revaluation ₹4,800; *C*'s Loan A/c ₹18,200; Capitals *A* ₹49,200; *B* ₹32,800; B/S total ₹1,22,800.]

Q. 17. Manoj, Naveen and Deepak were partners sharing profits and losses in the ratio of 4 : 3 : 2. As at April, 2020, their Balance Sheet was as follows :

Liabilities		₹	Assets		₹
Trade Creditors		7,000	Cash in Hand		5,900
Capitals :			Debtors	19,000	
Manoj	50,000		*Less* : Provision	1,400	17,600
Naveen	39,000		Stock		13,500
Deepak	30,000	1,19,000	Plant and Machinery		18,000
			Motor Car		20,000
			Buildings		48,000
			Goodwill		3,000
		1,26,000			1,26,000

Deepak retired on the above date as per the following terms :

1. Goodwill of the firm was valued at ₹21,000.
2. Stock to be appreciated by 10%.
3. Provision for doubtful debts should be 5% on debtors.
4. Machinery is to be valued at 5% more than its book value.
5. Motor Car is revalued at ₹15,500. Retiring partner took over Motor Car at this value.
6. Deepak be paid ₹2,000 in cash and balance be transferred to his loan account.

Show necessary journal entries. Prepare Revaluation Account, Capital Accounts and Opening Balance Sheet of continuing partners.

[**Ans.** Loss on Revaluation ₹1,800; Deepak's Loan A/c ₹16,100; Capitals : Manoj ₹45,200; Naveen ₹35,400; B/S total ₹1,03,700.]

Hint : Goodwill amounting to ₹3,000 will be written off among old partners in old ratio and Deepak's share in ₹21,000 will be debited to the accounts of Manoj and Naveen in gaining ratio *i.e.*, 4 : 3.

Q. 18. Anita, Gaurav and Sonu were partners in a firm sharing profits and losses in proportion to their capitals. Their Balance Sheet as at 31st March, 2019 was as follows :

BALANCE SHEET OF ANITA, GAURAV AND SONU

as at 31st March, 2019

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Capitals :			Land and Building		5,00,000
Anita	2,00,000		Investments		1,20,000
Gaurav	2,00,000		Debtors	1,50,000	
Sonu	1,00,000	5,00,000	*Less* : Provision for		
Investment Fluctuation Reserve		40,000	Doubtful Debts	10,000	1,40,000
General Reserve		30,000	Stock		1,00,000
Creditors		4,60,000	Cash at Bank		1,70,000
		10,30,000			10,30,000

On the above date, Anita retired from the firm and the remaining partners decided to carry on the business. It was agreed to revalue the assets and reassess the liabilities as follows :

(*i*) Goodwill of the firm was valued at ₹3,00,000 and Anita's share of goodwill was adjusted in the capital accounts of the remaining partners, Gaurav and Sonu.

(*ii*) Land and Building was to be brought up to 120% of its book value.

(*iii*) Bad Debts amounted to ₹20,000. A provision for doubtful debts was to be maintained at 10% on debtors.

(*iv*) Market value of investments was ₹1,10,000.

(*v*) ₹1,00,000 was paid immediately by cheque to Anita out of the amount due and the balance was to be transferred to her loan account which was to be paid in two equal annual instalments along with interest @ 10% p.a.

Prepare necessary journal entries on 31st March, 2019.

(C.B.S.E. 2020, Kolkata, Lucknow)

[**Ans.** Profit on Revaluation ₹77,000; Amount transferred to Anita's Loan A/c ₹2,74,800.]

Q. 19. Balance Sheet of *P*, *Q* and *R* who were sharing profits in proportion to their capitals stood as follows on 31st March, 2022 :

Liabilities	₹	*Assets*	₹
Sundry Creditors	70,000	Land & Buildings	1,00,000

Capital Accounts :			Machinery	1,70,000
P	1,00,000		Inventory	50,000
Q	1,50,000		Sundry Debtors	60,000
R	1,00,000	3,50,000	Cash at Bank	56,000
Current Accounts :			*R*'s Current A/c	10,000
P	20,000			
Q	6,000	26,000		
		4,46,000		4,46,000

Q retired on this date and the following was agreed upon :

(*i*) Inventory is overvalued by ₹5,000.

(*ii*) Land and Buildings are undervalued by ₹30,000.

(*iii*) Machinery be depreciated by 20%.

(*iv*) Provision for doubtful debts be made at 5%.

(*v*) Old credit balances of Sundry Creditors ₹5,000 be written back.

(*vi*) Some investments of the firm (not mentioned in the Balance Sheet) are taken over by *P* for ₹35,000.

(*vii*) Goodwill of the firm is valued at 63,000.

P and *R* decided to share the future profits and losses in the ratio of 3 : 2. It was further agreed that the amount due to *Q* in his Current Account be paid in cash and the remaining balance should be transferred to his Loan Account.

Prepare Revaluation Account, Capital and Current Accounts of the partners (assuming all adjustments to be made through Current Accounts) and the Balance Sheet of *P* and *R* after *Q*'s retirement.

[**Ans.** Profit on Revaluation ₹28,000; *Q*'s Current Account paid in Cash ₹45,000; *Q*'s Loan Account ₹1,50,000; Capital Accounts *P* and *R* ₹1,00,000 each. Current Account of *P* ₹26,800 (Dr.) and *R* ₹9,200 (Dr.); B/S Total ₹4,15,000.]

Q. 20. Sameer, Yasmin and Saloni were partners in a firm sharing profits and losses in the ratio of 4 : 3 : 3. On 31.3.2016, their Balance Sheet was as follows :

BALANCE SHEET OF SAMEER, YASMIN AND SALONI

as at 31.3.2016

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Creditors		1,10,000	Cash		80,000
General Reserve		60,000	Debtors	90,000	
Capitals :			*Less* : Provision	10,000	80,000
Sameer	3,00,000		Stock		1,00,000
Yasmin	2,50,000		Machinery		3,00,000
Saloni	1,50,000	7,00,000	Building		2,00,000
			Patents		60,000
			Profit and Loss Account		50,000
		8,70,000			8,70,000

On the above date, Sameer retired and it was agreed that :

(i) Debtors of ₹4,000 will be written off as bad debts and a provision of 5% on debtors for bad and doubtful debts will be maintained.

(ii) An unrecorded creditor of ₹20,000 will be recorded.

(iii) Patents will be completely written off and 5% depreciation will be charged on stock, machinery and building.

(iv) Yasmin and Saloni will share future profits in the ratio of 3 : 2.

(v) Goodwill of the firm on Sameer's retirement was vlaued at ₹5,40,000.

Pass necessary journal entries for the above transactions in the books of the firm on Sameer's retirement. *(C.B.S.E. 2017. Outside Delhi)*

[**Ans.** Loss on Revaluation ₹1,08,300; Amount transferred to Sameer's Loan A/c ₹4,76,680]

Hint. Entry for Bad-Debts and Provision for Bad Debts :

Provision for Bad Debts A/c	Dr.	5,700	
To Debtors A/c			4,000
To Revaluation A/c			1,700

Q. 21. Following is the Balance Sheet of *X, Y* and *Z* as at 31st March, 2022. They shared profits in the ratio of 3 : 3 : 2.

Liabilities		₹	*Assets*		₹
Sundry Creditors		2,50,000	Cash at Bank		50,000
General Reserve		80,000	Bills Receivable		60,000
Partners Loan A/cs :			Debtors	80,000	
X		50,000	*Less* : Provision for		
Y		40,000	Bad Debts	4,000	76,000
Capital A/cs :			Stock		1,24,000
X	1,00,000		Fixed Assets		3,00,000
Y	60,000		Advertisement Suspense A/c		16,000
Z	50,000	2,10,000	Profit and Loss A/c		4,000
		6,30,000			6,30,000

On 1st April, 2022 *Y* decided to retire from the firm on the following terms :

(a) Stock to be depreciated by ₹12,000.

(b) Advertisement Suspense Account to be written off.

(c) Provision for Bad and Doubtful Debts to be increased to ₹6,000.

(d) Fixed Assets be appreciated by 10%.

(e) Goodwill of the firm be valued at ₹80,000 and the amount due to the retiring partner be adjusted in *X*'s and *Z*'s Capital Accounts.

Prepare the Revaluation Account, Partner's Capital Accounts and the Balance Sheet to give effect to the above.

[**Ans.** Profit on Revaluation ₹16,000; *Y*'s Loan A/c ₹1,58,500 (*i.e.* ₹40,000 + ₹1,18,500); Capitals *X* ₹1,10,500 and *Z* ₹57,000; B/S Total ₹6,26,000.]

Q. 22. *A*, *B* and *C* are in partnership sharing profits in the ratio of 3 : 2 : 1. On 28th February, 2022 *C* retires from the firm. Their Balance Sheet as at that date was as follows:

Liabilities		₹	*Assets*	₹
Sundry Creditors		1,20,000	Bank	25,000
Outstanding Expenses		10,000	Debtors	1,65,000
Profit & Loss Account		1,50,000	Stock	2,50,000
Capital Accounts :			Investments	3,00,000
A	5,00,000		Fixed Assets	5,40,000
B	3,00,000			
C	2,00,000	10,00,000		
		12,80,000		12,80,000

The following was agreed upon :

(*i*) Goodwill of the firm is valued at ₹1,50,000. *C* sells his share of goodwill to *A* and *B* in the ratio of 4 : 1.

(*ii*) Stock is revalued at ₹3,00,000 and debtors are revalued at ₹1,50,000.

(*iii*) Outstanding expenses be brought down to ₹3,000.

(*iv*) Investments are sold at a loss of 10%.

(*v*) *C* is paid off in full.

Prepare Revaluation Account, Capital Accounts and the Balance Sheet of the new firm.

[**Ans.** Profit on Revaluation ₹12,000; Amount paid to *C* ₹2,52,000; *A*'s Capital ₹5,61,000; *B*'s Capital ₹3,49,000; B/S Total ₹10,33,000; Bank balance ₹43,000.]

Q. 23. Anand, Bihari and Shivin are equal partners in a firm. Bihari retires and his claim including his capital and his share of goodwill is ₹40,000. He is paid in kind, a vehicle valued at ₹20,000 which is unrecorded in the books of the firm till the date of retirement and the balance in cash.

You are required to give the journal entries for recording the payment to Bihari in the books of the firm. *(I.S.C. Sample Question Paper 2015)*

[**Ans.** Amount due to Bihari is settled by giving him vehicle valued ₹20,000 and ₹26,667 in cash.]

Q. 24. The Balance Sheet of *A*, *B* and *C* who were sharing profits in proportion to 2 : 1 : 1 stood as follows as at 31st March, 2022 :

Liabilities		₹	*Assets*	₹
Creditors		84,000	Cash at Bank	35,000
Reserve		26,000	Debtors	1,80,000
Capital Accounts :			Stock	2,15,000
A	3,00,000		Fixed Assets	4,20,000
B	2,00,000			
C	2,00,000	7,00,000		
Profit for the year 2021 – 22		40,000		
		8,50,000		8,50,000

The above balance sheet is wrong, since C has retired with effect from 1st January 2022. No adjustments have been made in the books on C's retirement.

You are required to make them and redraft the Balance Sheet. The Goodwill of the firm was valued at ₹72,000.

[**Ans.** C's Loan A/c ₹2,35,480; Capital Accounts : A ₹3,20,347 and B ₹2,10,173. Total of Balance Sheet ₹8,50,000.]

Hint : After 1st January 2022, C will be entitled (at his option) to either of the following :

(*i*) Interest at 6% p.a. for 3 months, *i.e.* $2,32,000 \times \frac{6}{100} \times \frac{3}{12} =$ ₹3,480; or

(*ii*) Profit which has been earned by the firm with the help of the amount due to him, *i.e.* $\frac{2,32,000}{7,56,000} \times$ ₹10,000 = ₹3,069.

Hence, he will opt for the first alternative.

Adjustment of Capitals

Q. 25. On 31st March, 2015, the Balance Sheet of Saman, Harish and Meeta who were sharing profits and losses in the ratio of 2 : 3 : 2, stood as follows :

BALANCE SHEET

as at 31st March, 2015

Liabilities		₹	*Assets*	₹
Capitals :	Saman 10,00,000		Land and Buildings	19,00,000
	Harish 15,00,000		Machinery	5,00,000
	Meeta 10,00,000	35,00,000	Furniture	7,70,000
Workmen Compensation Reserve		8,40,000	Closing Stock	5,00,000
Sundry Creditors		5,10,000	Sundry Debtors	7,00,000
			Cash	4,80,000
		48,50,000		48,50,000

On 31st March, 2015, Harish retired from the firm and the remaining partners decided to carry on the business. It was agreed to revalue the assets and liabilities as follows :

(*i*) Land and buildings be appreciated by 20%.

(*ii*) Machinery be depreciated by 20%.

(*iii*) Closing stock be valued at ₹4,50,000.

(*iv*) Provision for Doubtful Debts be made at 5% on Debtors.

(*v*) Sundry creditors of ₹65,000 be written off.

(*vi*) Goodwill of the firm be valued at ₹5,60,000 and Harish's share of the goodwill be adjusted in the accounts of Saman and Meeta who will share the future profits and losses in the ratio of 3 : 2.

(*vii*) The total capital of the newly constituted firm will be ₹35,00,000, which will be adjusted by opening Current Accounts.

(*viii*) Amount due to Harish was settled by accepting a bill of exchange in his favour payable after 4 months.

Prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet of the new firm on Harish's retirement. (C.B.S.E. 2016 Comptt. Delhi)

[**Ans.** Profit on Revaluation ₹2,60,000; Bills Payable accepted ₹22,11,428; Capital A/cs : Saman ₹21,00,000 and Meeta ₹14,00,000; Current A/cs Saman (Dr.) ₹9,61,714 and Meeta (Dr.) ₹1,49,714; B/S Total ₹61,56,428.]

Q. 26. *A*, *B* and *C* are partners sharing profits in the ratio of 1/2 : 1/3 and 1/6 respectively. Their Balance Sheet as at 31st March, 2022 was as follows :

Liabilities		₹	*Assets*		₹
Creditors		1,60,000	Land & Buildings		4,00,000
Provision for Legal Damages		40,000	Computers		40,000
Expenses Owing		10,000	Stock		1,40,000
Capital A/cs :			Sundry Debtors	80,000	
A	3,40,000		*Less* : Provision for		
B	1,50,000		Doubtful Debts	4,000	76,000
C	1,40,000	6,30,000	Cash at Bank		1,69,000
			Advertisement Expenditure		15,000
		8,40,000			8,40,000

B retired on 1st April 2022 and the new ratio between *A* and *C* was agreed at 3 : 2. The following were agreed :

(*i*) Goodwill of the firm is valued at ₹1,50,000.

(*ii*) Land & Buildings are to be increased by 10%.

(*iii*) Provision for Doubtful Debts is to be increased by ₹6,000.

(*iv*) Out of the insurance premium of ₹10,000 which was entirely debited to Profit and Loss Account, ₹2,000 be carried forward as unexpired insurance.

(*v*) Creditors will be written back by ₹20,000.

(*vi*) Part of the stock which had been included at cost of ₹10,000 had been badly damaged in storage and could only expect to realise ₹2,000.

(*vii*) Total capital of the new firm will be ₹5,00,000 and will be in the new profit sharing ratio of continuing partners. *B* will be paid ₹1,50,000 on retirement and the balance after six months.

Prepare Revaluation Account, Capital Accounts and the Balance Sheet of the new firm.

[**Ans.** Profit on Revaluation ₹48,000; *B*'s Loan ₹61,000; Final Capitals *A* ₹3,00,000 and *C* ₹2,00,000. *A* withdraws ₹41,500 and *C* brings in ₹89,500; Balance Sheet Total ₹7,51,000; Bank Balance ₹67,000.

Hint. Gaining Ratio 3 : 7.

Retirement and Settlement of Loan

Q. 27. *A*, *B* and *C* are partners sharing profits in 4 : 3 : 3. Their Balance Sheet as at 31st March 2022 was as follows :

Liabilities	₹	*Assets*	₹
Sundry Creditors	1,20,000	Land and Building	5,00,000

General Reserve		40,000	Stock		2,40,000
Capital Accounts :			Debtors	1,50,000	
A	4,00,000		*Less :* Provision for		
B	2,00,000		Doubtful		
C	2,00,000	8,00,000	Debts	30,000	1,20,000
			Cash at Bank		1,00,000
		9,60,000			9,60,000

C retires on 1st April, 2022 and *A* and *B* decide to share future profits in the ratio of 6 : 4. It is agreed that :

(*i*) Goodwill of the firm is valued at ₹80,000.

(*ii*) Land & Building is undervalued by ₹1,00,000 and Stock is overvalued by 20%.

(*iii*) Provision for Doubtful Debts is to be decreased to ₹10,000.

(*iv*) Computer valued ₹30,000 was unrecorded in the books.

It was decided to pay off *C* by giving him this computer and the balance in annual instalments of ₹1,00,000 together with interest @ 10% p.a.

You are required to prepare :

(*a*) Revaluation Account,

(*b*) *C*'s Capital Account, and

(*c*) *C*'s Loan Account till it is finally closed.

[**Ans.** Profit on Revaluation ₹1,10,000; Balance of *C*'s Capital A/c transferred to his Loan A/c ₹2,39,000. Payments made : ₹1,23,900 on 31st March 2023; ₹1,13,900 on 31st March 2024 and ₹42,900 on 31st March 2025.]

Q. 28. Lalit, Madhur and Neena were partners sharing profits as 50%, 30% and 20% respectively. On 31st March, 2020, their Balance Sheet was as follows :

Liabilities		₹	*Assets*		₹
Creditors		28,000	Cash		34,000
Provident Fund		10,000	Debtors	47,000	
Investment Fluctuation Fund		10,000	*Less* : Provision for Bad		
Capital A/cs :			and Doubtful Debts	3,000	44,000
Lalit	50,000		Stock		15,000
Madhur	40,000		Investment		40,000
Neena	25,000	1,15,000	Goodwill		20,000
			Profit and Loss A/c		10,000
		1,63,000			1,63,000

On this date, Madhur retired and Lalit and Neena agreed to continue on the following terms :

(*a*) The goodwill of the firm was valued at ₹51,000.

(*b*) There was a claim for Workmen's Compensation to the extent of ₹6,000.

(*c*) Investment were brought down to ₹15,000.

(*d*) Provision for bad debts was reduced by ₹1,000.

(*e*) Madhur was paid ₹10,300 in cash and the balance was transferred to his loan account payable in two equal instalments together with interest @12% p.a.

Prepare Revaluation Account, Partners' Capital Accounts and Madhur's Loan Account till the loan is finally paid off.

[**Ans.** Loss on Revaluation ₹20,000; Madhur's Loan A/c ₹30,000; Capital A/cs : Lalit ₹14,071 and Neena ₹10,629.]

Hint : Treatment of Investment Fluctuation Fund :

Investment Fluctuation Fund A/c	Dr.	10,000	
Revaluation A/c	Dr.	15,000	
To Investments A/c			25,000

Q. 29. *R*, *S* and *T* were partners in a firm sharing profits in 2 : 2 : 1 ratio. On 1-4-2021 their Balance Sheet was as follows :

Liabilities		₹	*Assets*	₹
Bank Loan		12,800	Cash	51,300
Sundry Creditors		25,000	Bills Receivable	10,800
Capitals :			Debtors	35,600
R	80,000		Stock	44,600
S	50,000		Furniture	7,000
T	40,000	1,70,000	Plant and Machinery	19,500
Profit and Loss A/c		9,000	Building	48,000
		2,16,800		2,16,800

S retired from the firm on 1-4-2021 and his share was ascertained on the revaluation of assets as follows :

Stock ₹40,000; Furniture ₹6,000; Plant and Machinery ₹18,000; Building ₹40,000; ₹1,700 were to be provided for doubtful debts. The goodwill of the firm was valued at ₹12,000.

S was to be paid ₹21,680 in cash on retirement and the balance in three equal quarterly instalments (starting from 30th June 2021) alongwith interest @ 12% p.a.

Prepare Revaluation Account, Partner's Capital Accounts, *S*'s Loan Account and Balance Sheet on 1-4-2021.

[**Ans.** Loss on Revaluation ₹16,800; *S*'s Loan A/c ₹30,000; Capital A/cs : *R* ₹73,680 and *T* ₹36,840; Balance Sheet Total ₹1,78,320.]

Hint : Payment of *S*'s Loan A/c : ₹10,900 on 30th June 2021; ₹10,600 on 30th Sept. 2021 and ₹10,300 on 31st Dec. 2021.

Q. 30. *P*, *Q* and *R* were partners sharing profits and losses in the ratio of 5 : 3 : 2 respectively. On 31st March, 2020 the Balance Sheet of the firm stood as follows :

Liabilities		₹	*Assets*	₹
Sundry Creditors		5,300	Fixed Assets	25,000
Expenses Outstanding		700	Stock	11,000
Reserve		3,000	Book Debts	9,000
Capitals :			Cash at Bank	2,000
P	20,000			

Q	10,000			
R	8,000	38,000		
		47,000		47,000

On this date *Q* decided to retire and for this purpose :

(*a*) Goodwill was valued at ₹19,000;

(*b*) Fixed assets were valued at ₹30,000;

(*c*) Stock was considered as worth ₹10,000.

Q was to be paid through cash, brought in by *P* and *R*, in such a way as to make their capitals proportionate to their new profit sharing ratio which was to be *P* 3/5 and *R* 2/5.

Record these matters in the journal of the firm and prepare the resultant Balance Sheet.

[**Ans.** Profit on revaluation ₹4,000; Amount paid to *Q* ₹17,800; Capital A/cs: *P* ₹27,000, *R* ₹18,000 and Balance Sheet total ₹51,000; Gaining Ratio 1 : 2.]

Hints : Total Capital of the new firm = ₹21,600 + ₹17,800 + ₹5,600 = ₹45,000

P's Capital in the new firm = ₹45,000 × $\frac{3}{5}$ = ₹27,000

R's Capital in the new firm = ₹45,000 × $\frac{2}{5}$ = ₹18,000

Cash brought in by *P* = ₹27,000 – ₹21,600 = ₹ 5,400

Cash brought in by *R* = ₹18,000 – ₹ 5,600 = ₹12,400

Q. 31. *P*, *Q* and *R* are partners in a firm. *R* retires from the firm. On the date of retirement, ₹3,00,000 is due to him. It is agreed to pay him in instalments every year at the end of the year. Prepare *R*'s Loan Account in the following cases :

(*i*) Five yearly instalments plus interest @ 15% p.a.

(*ii*) Instalments of ₹1,00,000 which already include interest @ 15% p.a. on the outstanding balance for the first four years and the balance including interest in the fifth year.

[**Ans. First Method :** Interest : Ist year ₹45,000; IInd year ₹36,000; IIIrd year ₹27,000; IVth year ₹18,000; Vth year ₹9,000;

Second Method : Interest : Ist year ₹45,000; IInd year ₹36,750; IIIrd year ₹27,263; IVth year ₹16,352; Vth year ₹3,805; Final Payment ₹29,170]

Q. 32. *A*, *B* and *C* are partners in a firm sharing profits in the ratio of 3 : 2 : 1. On 31st March 2022 *C* retired. Following balances were disclosed by the Firm's Balance Sheet on this date :

(*i*) Capitals : *A* ₹10,00,000; *B* ₹6,00,000 and *C* ₹4,40,000.

(*ii*) Profit & Loss (Dr. Balance) ₹45,000.

(*iii*) Advertisement Expenditure ₹15,000.

Revaluation of Assets and re-assessment of liabilities resulted in a loss of ₹60,000. On the retirement of C, goodwill is valued at ₹1,80,000.

The amount payable to C is agreed to be paid in two yearly instalments of ₹2,00,000 each including intrest @ 10% p.a. on the outstanding balance during the first two years and the balance including interest in the third year. Books are closed on 31st March every year.

Prepare C's Loan Account till it is finally paid.

[**Ans.** Net amount payable to C ₹4,50,000; Payment made in third year ₹1,36,950 (including interest)]

Q. 33. X, Y and Z were partners sharing profits and losses in the ratio of 3 : 2 : 1 respectively. Their capital accounts showed the following balances :

	₹
X	1,80,000
Y	1,50,000
Z	1,20,000

Z retired on 31st March, 2022. All the partners agreed to revalue certain assets as follows :

	Book value as on 31st March, 2022	*Revised Value*
Plant & Machinery	1,22,000	1,30,000
Furniture	90,000	88,000

Goodwill was agreed to be valued at ₹54,000. Z's current account at the date of retirement showed a credit balance of ₹11,000. At the date of retirement Z was given ₹75,000 in cash and the balance were transferred to his loan account and were repaid (at the end of each year) in four equal instalments plus interest at 6% per annum on the annual balance.

After Z's retirement, profits were to be shared in the ratio of 2 : 1 and all assets (except goodwill) would appear at their revised values.

You are required to show the Partnership Accounts giving effect to these transactions.

[**Ans.** Profit on Revaluation ₹6,000; Balance of X's Capital A/c ₹1,74,000; Y's Capital A/c ₹1,52,000 and amount transferred to Z's Loan A/c ₹66,000; Interest on Z's loan 1st year ₹3,960, 2nd year ₹2,970, 3rd year ₹1,980, 4th year ₹990]

Q. 34. A, B and C are partners sharing profits in the proportion of 5 : 3 : 2. A retires from the firm on 31st March, 2014 and you are informed that :

(*i*) A's capital on 1st April, 2013 stood at ₹5,00,000 and interest on capital is to be allowed @ 8% p.a.

(*ii*) A has withdrawn ₹5,000 per month at the beginning of each month during the year 2013-14. Interest on drawings is to be charged @ 12% p.a.

(*iii*) A's share of profit for the year 2013-14 (after all adjustments) amounts to ₹75,000.

(*iv*) Goodwill of the firm is worth ₹1,00,000.

B and *C* decide to share future profits equally. The amount due to *A* in excess of ₹5,00,000 is to be paid in cash immediately on retirement and the balance due to him is to be paid in annual instalments of ₹2,50,000 each, interest being calculated @ 12% p.a. on the unpaid balances. The first instalment was paid on 31st March 2015.

You are required to prepare *A*'s Capital Account and also his Loan Account until the payment of the whole amount due to him was made.

[**Ans.** Amount paid to *A* in Cash ₹1,01,100; Interest due on 31st March 2015 ₹60,000, on 31st March 2016 ₹37,200 and on 31st March 2017 ₹11,664. Amount paid on 31st March 2015 ₹2,50,000; On 31st March 2016 ₹2,50,000 and on 31st March 2017 ₹1,08,864.]

Hint : *A*'s share of Goodwill ₹50,000 will be debited to *B* and *C* in their gaining ratio of 2 : 3.

Q. 35 (A). The Balance Sheet of *A, B* and *C*, who were sharing profit and losses in the proportion of their capitals, as at 31st March, 2020 was as follows :

Liabilities	₹	*Assets*		₹
Sundry Creditors	3,500	Cash		2,700
Capitals :		Debtors	3,000	
A	15,000	*Less* : Provision for		
B	12,000	Doubtful Debts	200	2,800
C	9,000	Stock		5,000
		Machinery		14,000
		Building		15,000
	39,500			39,500

B retired on 1st April, 2020 and the following adjustments were made :

(*i*) Building be appreciated by 20%, stock be depreciated by 10%, provision for doubtful debts be maintained at 5% and a provision for legal charges be created at ₹450.

(*ii*) The goodwill of the firm be fixed at ₹6,000 and *B*'s share be adjusted into *A* and *C* capital accounts.

(*iii*) ₹12,000 from *B*'s capital account be transferred to his loan account and balance be paid in cash, and

(*iv*) The capital of the new firm of *A* and *C* be fixed at ₹25,000 and the profit sharing ratio at 3 : 2. Capital accounts of partners be adjusted accordingly and any surplus or deficit be transferred to current accounts.

Prepare Revaluation Account, Capital Accounts and Balance Sheet of *A* and *C*.

[**Ans.** Profit on revaluation ₹2,100; Cash paid to *B* ₹2,700; Amount transferred to current accounts *A* ₹225 (Dr.) and *C* ₹1,375 (Dr.); Cash Balance Nil, Capital Accounts *A* ₹15,000 and *C* ₹10,000 and Balance Sheet total ₹40,950. Gaining Ratio 11 : 9.]

Q. 35 (B). Kushal, Kumar and Kavita were partners in a firm sharing profits in the ratio of 3 : 1 : 1. On 1st April, 2020 their Balance Sheet was as follows :

BALANCE SHEET OF KUSHAL, KUMAR AND KAVITA
as at 1st April, 2020

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Creditors		1,20,000	Cash		70,000
Bills Payable		1,80,000	Debtors	2,00,000	
General Reserve		1,20,000	*Less* : Provision	10,000	1,90,000
Capitals :			Stock		2,20,000
Kushal	3,00,000		Furniture		1,20,000
Kumar	2,80,000		Building		3,00,000
Kavita	3,00,000	8,80,000	Land		4,00,000
		13,00,000			13,00,000

On the above date Kavita retired and the following was agreed :

(*i*) Goodwill of the firm was valued at ₹40,000.

(*ii*) Land was to be appreciated by 30% and building was to be depreciated by ₹1,00,000.

(*iii*) Value of furniture was to be reduced by ₹20,000.

(*iv*) Bad debts provision is to be increased to ₹15,000.

(*v*) 10% of the amount payable to Kavita was paid in cash and the balance was transferred to her Loan Account.

(*vi*) Capitals of Kushal and Kumar will be in proportion to their new profit sharing ratio. The surplus/deficit, if any in their Capital Accounts will be adjusted through Current Accounts.

Prepare Revaluation Account, Partner's Capital Accounts and Balance Sheet of Kushal and Kumar after Kavita's retirement.

[**Ans.** Loss on Revaluation ₹5,000; Kavita's Loan Account ₹2,97,900; Capital A/cs : Kushal ₹4,98,000; Kumar ₹1,66,000; Current A/cs : Kushal ₹1,35,000 (Dr.); Kumar ₹1,35,000 (Cr.); Balance Sheet Total ₹13,96,900.]

Q. 36. *A*, *B* and *C* were partners sharing profits and losses in 3 : 4 : 2. The following is the Balance Sheet of *A*, *B* and *C* as at 31st March, 2022 :

Liabilities		₹	*Assets*	₹
Creditors		75,000	Fixed Assets	3,20,000
Profit and Loss A/c :			Stock	1,40,000
Opening Balance	18,000		Debtors	1,13,000
Profit for the Year	72,000	90,000	Cash at Bank	1,80,000
Capital Accounts :			Advertisement Suspense	27,000
A	2,00,000			
B	2,50,000			
C	1,65,000	6,15,000		
		7,80,000		7,80,000

Owing to falling health *B* retired on 30th June, 2022. It is agreed that :

(i) The retiring partner shall be paid his share of profit in proportion to the period he served as a partner in the year of retirement. For this purpose, profit of the immediately preceding year will be taken as base.

(ii) The retiring partner will be entitled to his share of goodwill calculated at 3 times of the four year's average profits. The profits for the year ending 31st March 2019, 2020 and 2021 were ₹32,000, ₹60,000 and ₹52,000 respectively.

(iii) *A* and *C* will share future profits in the ratio of 5 : 3.

(iv) Capital accounts of *A* and *C* will be readjusted by bringing in or paying out cash so that their capitals become in the new profit sharing ratio. ₹1,58,000 from *B*'s Capital Account will be paid in cash and the balance will be transferred to his Loan Account.

Prepare Journal entries, Capital Accounts and a Balance Sheet as at that date.

[**Ans.** Sacrificing Ratio 21 : 11; *B*'s share of Goodwill ₹72,000. *B*'s Loan A/c ₹2,00,000; Capitals Accounts *A* ₹2,00,000 and *C* ₹1,20,000; *A* brings in ₹31,500 and *C* withdraws ₹31,500; B/S Total ₹5,95,000.]

Q. 37. *A*, *B* and *C* are partners sharing profits and losses in the ratio of 2 : 2 : 1. The Balance Sheet of their business as at 31st March 2022 is given below :

Liabilities	₹	*Assets*		₹
Sundry Creditors	90,000	Machinery at Cost	3,00,000	
Capital Accounts :		*Less* : Provision for		
A	1,70,000	Depreciation	60,000	2,40,000
B	2,30,000	Office Equipment		50,000
C	1,50,000	Stock		1,70,000
		Investments		50,000
		Debtors	1,20,000	
		Less : Provision	6,000	1,14,000
		Cash at Bank		16,000
	6,40,000			6,40,000

C retired on 31st July 2022 and *A* and *B* decided to share future profits in the ratio of 2 : 3.

The terms of retirement provide the following :

(i) Machinery was to be revalued at ₹2,25,000.

(ii) Liability for the payment of gratuity to workers ₹16,000 is to be provided for.

(iii) Provision for bad debts is no more necessary.

(iv) Investments are to be taken over by the retiring partner at ₹60,000.

(v) A provision for ₹5,000 be made in respect of an outstanding bill for repairs.

(vi) Goodwill of the firm is valued at ₹60,000 and profit upto the date of retirement was estimated at ₹40,000.

(vii) *C* was paid off in full and a bank loan of ₹1,00,000 is to be arranged for this purpose.

(viii) The capitals of A and B will be readjusted according to their new profit sharing ratio by bringing in or paying cash to the partners.

Prepare Revaluation Account, Capital Accounts of partners and the Balance Sheet of the new firm.

[**Ans.** Loss on Revaluation ₹20,000; Cash paid to C ₹1,06,000; Capital Accounts balances A ₹1,45,600 and B ₹2,18,400; A withdraws ₹16,400 and B brings in ₹16,400; Bank balance ₹10,000; Balance Sheet Total ₹5,75,000.]

Hints : (i) C's share of goodwill ₹12,000 will be debited to B's Capital Account as he alone has gained on C's retirement.

(ii) Since the profit sharing ratio of continuing partners does not remain the same, C's share of profit upto the date of retirement will be debited to B's Capital Account, since he alone has gained on C's retirement.

Q. 38. P, Q and R are in partnership sharing profits in the ratio of 3 : 2 : 1. R retires. Following balances appeared in their books :

		₹	₹
Goodwill		12,000	
Bank		10,000	
Other Assets		70,000	
Creditors			14,000
Capitals :	P		40,000
	Q		20,000
	R		18,000
		92,000	92,000

Goodwill is agreed at ₹30,000. Sufficient money is to be introduced so that R is paid off and leave ₹4,000 in cash at bank. P and Q are to provide such sum as will make their capitals proportionate to their share of profits.

Prepare necessary entries and the new balance sheet.

[**Ans.** Amount paid to R ₹21,000; Final Capitals P ₹36,000; Q ₹24,000. P brings in ₹5,000 and Q ₹10,000. B/S total ₹74,000.]

Q. 39. X, Y and Z are partners sharing profits in the ratio of 4 : 2 : 3. Y retires. On this date his Capital after making adjustments for reserves and revaluation exists at ₹2,00,000. X and Z agreed to pay him ₹2,40,000 in full settlement of his account. Record necessary journal entry for the treatment of goodwill if X and Z decided to share future profits equally.

[**Ans.** Hidden Goodwill ₹40,000. It will be debited to X and Z in their gaining ratio 1 : 3.]

Death of a Partner

Q. 40. A, B and C were partners in a firm. B died on 31st August, 2022. B's share of profit from the closure of the last accounting year till the date of death was to be calculated on the basis of the average of three completed years of profits before death. Profits for the years ending 31st March 2020, 2021 and 2022 were ₹40,000; ₹50,000 and ₹72,000 respectively. The firm closes its books on 31st March every year.

Calculate *B*'s share of profit till the date of her death and pass the necessary journal entry for the same assuming :

(*i*) There is no change in the profit sharing ratio of *A* and *C*

(*ii*) There is change in the profit sharing ratio of *A* and *C* and the new ratio is 7 : 5.

[**Ans.**

Case (*i*)	P & L Suspense A/c	Dr.	7,500	
	To *B*'s Capital A/c			7,500
Case (*ii*)	*A*'s Capital A/c	Dr.	5,625	
	C's Capital A/c	Dr.	1,875	
	To *B*'s Capital A/c			7,500]

Q. 41. Hari, Mohan and Sohan were partners in a firm sharing profits in 2 : 2 : 1 ratio. The firm closes its books on 31st March every year. Mohan died on 24-8-2021. On Mohan's death the goodwill of the firm was valued at ₹75,000. The partnership deed provided that on the death of a partner his share in the profits of the firm in the year of his death will be calculated on the basis of last year's profit. The profit of the firm for the year ended 31-3-2021 was ₹2,00,000. Calculate Mohan's share of profit till the time of his death and pass the necessary journal entries for the treatment of goodwill and his share of profit.

[**Ans.** Mohan's share of goodwill ₹30,000; Mohan's share of profit ₹32,000.]

Hint : Number of Days up to the date of death = 146.

Q. 42. *A, B* and *C* are sharing profits in the ratio of 4 : 3 : 2. *A* dies on 31st December, 2019. Accounts are closed on 31st March every year. Sales for the year ending 31st March, 2019 amounted to ₹4,00,000. Sales of ₹3,30,000 amounted between the period from 1st April, 2019 to 31st December, 2019. The profit for the year ending 31st March, 2019 amounted to ₹60,000.

Calculate the deceased partner's share in the current year's profits of the firm.

[**Ans.** ₹22,000]

Q. 43. *A, B* and *C* were partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1. Their books are closed on March 31st every year.

B died on 1st August, 2019. The executors of *B* are entitled to :

(*i*) His share of Capital *i.e.*, ₹4,00,000 along-with his share of goodwill. The total goodwill of the firm was valued at 1.5 year's purchase of last year's profit.

(*ii*) His share of profit up to his date of death on the basis of sales till date of death. Sales for the year ended March 31, 2019 was ₹4,00,000 and profit for the same year was ₹80,000. Sales shows a growth trend of 25% and percentage of profit earning is increased by 4%.

(*iii*) Amount payable to *B* was transferred to his executors.

Pass necessary Journal Entries and show the workings clearly.

Ans. Amount payable to *B*'s Executors ₹4,64,000

Hints : *B*'s share of Goodwill ₹48,000; *B*'s share of profit ₹16,000.

Q. 44. The Balance Sheet of Sindhu, Rahul and Kamlesh, who were sharing profits in the ratio of 3 : 3 : 4 respectively, as at 31st March, 2020 was as follows :

Liabilities		*Amount*	*Assets*	*Amount*
		₹		₹
General Reserve		10,000	Cash	32,000
Bills Payable		20,000	Stock	88,000
Loan		24,000	Investments	94,000
Capitals :	Sindhu : 1,20,000		Land & Building	1,20,000
	Rahul : 1,00,000		Sindhu's Loan	20,000
	Kamlesh : 80,000	3,00,000		
		3,54,000		3,54,000

Sindhu died on 31st July 2020. The partnership deed provided for the following on the death of a partner :

(*a*) Goodwill of the firm be valued at two year's purchase of average profits for the last three years which were ₹80,000.

(*b*) Sindhu's share of profit till the date of his death was to be calculated on the basis of sales. Sales for the year ended 31st March, 2020 amounted to ₹8,00,000 and that from 1st April to 31st July 2020 ₹3,00,000. The profit for the year ended 31st March, 2020 was ₹2,00,000.

(*c*) Interest on capital was to be provided @ 6% p.a.

Prepare Sindhu's Capital Account to be rendered to his executor.

[**Ans.** Balance due to Sindhu's Executor ₹1,75,900.]

Q. 45. *A*, *B* and *C* were partners in a firm sharing profits in the ratio of 5 : 3 : 2. The Balance Sheet as at 31-3-2020 was as follows :

Liabilities	₹	*Assets*	₹
Creditors	12,000	Building	20,000
Reserves	6,000	Plant and Machinery	16,000
A's Capital	24,000	Stock	5,100
B's Capital	12,000	Debtors	6,000
C's Capital	8,000	Cash at Bank	6,900
		Advertisement Suspense	8,000
	62,000		62,000

A died on 30-9-2020 and *B* and *C* decided to share future profits in the ratio of 7 : 3. Under the partnership agreement the executors of a deceased partner were entitled to :

(*a*) Amount standing to the credit of partner's capital account.

(*b*) Interest on capital at 12% per annum.

(*c*) Share of goodwill on the basis of four years purchase of last three years average profit.

(*d*) Share of profit from the closing of the last financial year to the date of death on the basis of last year's profit. Profits for the year 2018, 2019 and 2020 were ₹8,000; ₹12,000 and ₹7,000 respectively.

Prepare *A*'s Capital account to be rendered to his executors.

[**Ans.** Amount due to *A*'s Executor's ₹44,190.]

Hint : *A*'s share of goodwill ₹18,000 and share of profit ₹1,750 will be credited to *A* and debited to *B* and *C* in their gaining ratio of 4 : 1. *A*'s share of profit should not be debited to Profit & Loss Suspense A/c because profit sharing ratio between *B* and *C* does not remain the same. Their profit sharing ratio has changed from 3 : 2 to 7 : 3.

Q. 46. Ram, Ghanshyam and Vrinda were partners in a firm sharing profits in the ratio of 4 : 3 : 1. The firm closes its books on 31st March every year. On 1st February, 2015 Ghanshyam died and it was decided that the new profit-sharing ratio between Ram and Vrinda will be equal. The Partnership Deed provided for the following on the death of a partner :

(*a*) His share of goodwill be calculated on the basis of half of the profits credited to his account during the previous four completed years :
The firm's profit for the last four years were.
2010-11 — ₹1,20,000, 2011-12 — ₹80,000, 2012-13 — ₹40,000, and 2013-14 — ₹80,000.

(*b*) His share of profit in the year of his death was to be computed on the basis of average profits of past two years.

Pass necessary Journal entries relating to goodwill and profit to be transferred to Ghanshyam's Capital Account. Also show your workings clearly.

(C.B.S.E. 2016 Comptt. Delhi)

[**Ans.** Ghanshyam's share of Goodwill ₹60,000, which will be debited entirely to Vrinda's Capital A/c; Ghanshyam's share of profit till the date of death ₹18,750 will also be debited entirely to Vrinda's Capital A/c.]

Hint : Ghanshyam's share of profit will not be adjusted through Profit & Loss Suspense A/c because of change in profit sharing ratios of continuing partners.

Q. 47. *A*, *B* and *C* were partners in a firm. *A* died on 31.3.2018 and the Balance Sheet of the firm on that date was as under :

BALANCE SHEET OF *A*, *B* AND *C*
as at 31.3.2018

Liabilities		₹	*Assets*	₹
Creditors		7,000	Cash at Bank	12,000
General Reserve		9,000	Debtors	32,000
Workmen's Compensation Reserve		10,000	Furniture	30,000
Profit & Loss Account		6,000	Plant	40,000
Capitals :			Patents	8,000
A	40,000			
B	30,000			
C	20,000	90,000		
		1,22,000		1,22,000

On *A*'s death it was found that patents were valueless, furniture was to be brought down to ₹24,000, plant was to be reduced by ₹10,000 and there was a liability of ₹7,000 on account of workmen's compensation.

Pass the necessary journal entries for the above at the time of *A*'s death.
(C.B.S.E. 2019, Delhi)

[**Ans.** Amount due to *A*'s Executors ₹38,000.]

Q. 48. Tripti, Atishay and Radhika were partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1. Their Balance Sheet as at 31-3-2019 was as follows :

BALANCE SHEET OF TRIPTI, ATISHAY AND RADHIKA
as at 31st March, 2019

Liabilities		₹	*Assets*	₹
Capitals :			Plant and Machinery	5,00,000
Tripti	3,00,000		Stock	3,10,000
Atishay	2,00,000		Sundry Debtors	60,000
Radhika	1,00,000	6,00,000	Cash at Bank	40,000
Profit for the Year 2018-19		2,00,000		
General Reserve		50,000		
Creditors		60,000		
		9,10,000		9,10,000

Tripti died on 30th June, 2019. According to the partnership deed, the executors of the deceased partner are entitled to :

(*a*) Balance in partner's capital account.

(*b*) Salary @₹12,500 per quarter.

(*c*) Share of goodwill calculated on the basis of twice the average of past three years' profits and share of profits from the closure of the last accounting year till the date of death on the basis of last year's profit. Profits for 2016-17 and 2017-18 were ₹1,00,000 and ₹1,50,000 respectively.

(*d*) Tripti withdrew ₹20,000 on 1st May, 2019 for her personal use.

Prepare Tripti's Capital Account to be rendered to her executors.
(C.B.S.E. 2020, Delhi Modified)

[**Ans.** Amount due to Tripti's Executors ₹5,32,500.]

Hint : Average Profit = 1/3 (1,00,000 + 1,50,000 + 2,00,000 given in Balance Sheet.)

Q. 49. *A, B, C* and *D* were partners sharing profits in the ratio of 5 : 3 : 2 : 2. *B* died on 1st March, 2022. Goodwill of the firm was valued at ₹6,00,000. *A, C* and *D* decided to share future profits equally. Give necessary journal entry.

[**Ans.** Debit *C* and *D* by ₹1,00,000 each and Credit *A* by ₹50,000 and *B* by ₹1,50,000.]

Q. 50. Rita, Nina and Mita are partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. Mita dies on 1st April, 2017. On the date of her death, it was decided to value goodwill on the basis of two year's purchase of weighted average profits of the firm for the last three years.

The profits of the last three years and weights assigned were :

Year	*Profit (₹)*	*Weights assigned*
2014-15	30,000 (including gain from speculation ₹10,000)	1
2015-16	80,000	2
2016-17	1,00,000	3

You are required to :

(*i*) Calculate the firm's goodwill on the date of Mita's death (Show the working with the formula).

(*ii*) Pass the necessary journal entry to credit Mita's Capital Account with her share of goodwill. (*I.S.C. 2018*)

[**Ans.** Rita's Capital A/c	Dr.	16,000	
Nina's Capital A/c	Dr.	10,667	
To Mita's Capital A/c			26,667]

Q. 51 (A). Bina and Anita are partners. Their partnership agreement provides for the following :

(*i*) Accounts are to be balanced on 31st December each year :

(*ii*) Profits are to divided as follows :
Bina : one-half Anita : one third and carrried to Reserve Account : one sixth.

(*iii*) That in the event of death of a partner, her executors will be entitled to the following :

(*a*) The capital to her credit at the date of death.

(*b*) Proportionate profit to date of death based on the average profits of the last three completed years.

(*c*) Share of goodwill based on three years' purchases of the average profits for the three preceding completed years.

The profit for the three years were : year 2005 — ₹42,000; year 2006 — ₹39,000 and year 2007 — ₹45,000.

On 31.12.07, Anita's capital stood at ₹60,000 and firm's General Reserve Account stood at ₹30,000 Anita expired on 1.5.08.

From the above, prepare Anita's Executors Account as would appear in the firm's ledger transferring the amount to her Loan Account with proper working notes. (*I.S.C. 2009*)

[**Ans.** Balance due to Anita's Executors : ₹1,28,000.]

Q. 51 (B). *X* and *Y* shared profits in the ratio of 2 : 1. Following is their Balance Sheet as at 31st March, 2019 :

BALANCE SHEET

Liabilities	₹	*Assets*		₹
Creditors	6,200	Bank		10,800
Workmen Compensation Reserve	18,000	Debtors	10,000	
Capitals : *X*	50,000	*Less* : Provision	600	9,400

Y	27,000	B/R	2,000
		Goodwill	9,000
		Fixed Assets	70,000
	1,01,200		1,01,200

Y died on 30th June, 2019. Besides his capital and reserves, his legal representatives are entitled to :

I. His share of goodwill based on 2 years purchase of the last 3 years average profits less 10%. Last three years profits were ₹9,000; ₹20,000 and ₹16,000.

II. Fixed Assets are revalued at ₹76,000. There is no need of provision for doubtful debts, as the debtors are all good.

III. He is to be allowed interest at 12% p.a. upto the date of death.

Prepare *Y*'s A/c to be rendered to his legal representatives.

[**Ans.** Amount due ₹42,010.]

Q. 52. *A, B* and *C* are in partnership, sharing profits in the proportion of two-thirds, one-sixth and one-sixth respectively.

A died on the 30th June, 2020, three months after the annual accounts had been prepared and in accordance with the partnership agreement, his share of the profits to the date of death was estimated on the basis of the profit for the preceding year. In addition to this, the agreement provided for interest on capital at 5 per cent per annum on the balance standing to the credit of the capital account at the date of the last Balance Sheet, and also for goodwill, which was to be brought into account at two years' purchase of the average profits for the last three years.

A's capital on 31st March, 2020 stood at ₹1,20,000, and his drawings from then to the date of death amounted to ₹9,000.

The net profits of the business for the three preceding years amounted to ₹33,500; ₹41,500 and ₹40,500, respectively.

You are required to prepare *A*'s Capital Account as at the date of death, for a settlement with his executors.

[**Ans.** Amount payable to *A*'s executors ₹1,70,583].

Q. 53. You are given the Balance Sheet of *A, B* and *C* who are partners sharing profits in the ratio of 2 : 2 : 1 as at March 31, 2022.

Liabilities		₹	*Assets*	₹
Creditors		40,000	Goodwill	30,000
Reserve Fund		25,000	Fixed Assets	60,000
Capitals :			Stock	10,000
A	30,000		Sundry Debtors	20,000
B	25,000		Cash at Bank	15,000
C	15,000	70,000		
		1,35,000		1,35,000

B died on June 15, 2022. According to the Deed, his legal representatives are entitled to :

(a) Balance in Capital Account;

(b) Share of goodwill valued on the basis of thrice the average of the past 4 years' profits;

(c) Share in profits up to the date of death on the basis of average profits for the past 4 years;

(d) Interest on capital account @ 12% p.a.

Profits for the years ending on March 31 of 2019, 2020, 2021, 2022 respectively were ₹15,000, ₹17,000, ₹19,000 and ₹13,000.

B's legal representatives were to be paid the amount due. *A* and *C* continued as partners by taking over *B*'s share equally. Work out the amount payable to *B*'s legal representatives.

[**Ans.** Amount paid to *B*'s representatives ₹44,158.]

Hints : (1) Share in profits for 2.5 months ₹1,333.

(2) *B*'s share of profit ₹1,333 will be credited to *B* and debited to *A* and *C* in their gaining ratio *i.e.* equally.

Q. 54. Akhil, Nikhil and Sunil were partners sharing profits and losses equally. Following was their Balance Sheet as at 31st March, 2020.

Liabilities		₹	*Assets*	₹
Trade Creditors		40,000	Buildings	2,00,000
General Reserve		45,000	Plant & Machinery	80,000
Capitals :			Stock	35,000
Akhil	1,95,000		Debtors	80,000
Nikhil	1,20,000		Cash at Bank	85,000
Sunil	80,000	3,95,000		
		4,80,000		4,80,000

Sunil died on 1st August, 2020. The partnership deed provided that the executor of a deceased partner was entitled to :

(i) Balance of partner's capital account and his share of the accumulated reserves.

(ii) Share of goodwill calculated on the basis of three times the average profits of the last four years.

(iii) Share of profit from the closure of the last accounting year till the date of death on the basis of the profit of the preceding completed year before death.

(iv) Interest on deceased's capital @ 6% per annum.

₹50,000 to be paid to deceased's executor immediately and the balance to be kept in his loan account.

Profits and losses for the preceding years ending 31st March were :

2017 — ₹ 80,000 profit
2018 — ₹1,00,000 loss
2019 — ₹1,20,000 profit
2020 — ₹1,80,000 profit

Pass the necessary journal entries and prepare Sunil's Capital Account and Sunil's Executor's Account.

[**Ans.** Balance of Sunil's Executor's Account ₹1,36,600.]

Q. 55. *X*, *Y* and *Z* were partners sharing profits in the ratio of 3 : 2 : 1. On 31st March, 2020, their Balance Sheet stood as under :

Liabilities		₹	*Assets*	₹
Sundry Creditors		44,000	Cash at Bank	22,000
Reserve		90,000	Stock	1,20,000
Capitals :			Debtors	64,000
X	2,00,000		Investments	2,50,000
Y	1,50,000		Fixed Assets	1,28,000
Z	1,00,000	4,50,000		
		5,84,000		5,84,000

Y died on 31st July, 2020. The partnership deed provides that the executors of the deceased partner are entitled to :

(*i*) The Capital to his credit at the time of his death;

(*ii*) His share of reserves;

(*iii*) His share of profits to the date of death based on the average profits of the last three completed years, less 10%, and

(*iv*) Goodwill according to his proportion of the total profits for the three preceding years, which were ₹80,000; ₹1,30,000 and ₹1,50,000 respectively.

The Investments were sold at par and *Y*'s executor's were paid off.

Prepare Partner's Capital Accounts, *Y*'s Executor's Account and Balance Sheet of the surviving partners *X* and *Z*.

[**Ans.** Amount paid to *Y*'s executor's ₹3,12,000; *Y*'s share of profit ₹12,000; *Y*'s share of goodwill ₹1,20,000; *X*'s Capital ₹1,55,000 and *Z*'s Capital ₹85,000; Bank Loan ₹40,000; Total of Balance Sheet ₹3,24,000.]

Q. 56. *A*, *B* and *C* are equal partners of a trading firm. The capital of the firm on 1st April, 2020 is ₹6,00,000 held equally by the partners.

Under the Partnership Deed :

(*a*) *A* and *B* were entitled to be credited at the close of each year with partnership salaries of ₹1,000 p.m. and ₹1,500 p.m. respectively.

(*b*) In the event of death of a partner, Goodwill is to be valued at one year's purchase of average profit of the three years preceding the death.

(*c*) Partners were to be charged 6% p.a. interest on their drawings and were to be allowed 6% p.a. interest on their capitals.

B died on 30th June, 2020. His drawings from 1st April to 30th June 2020 amounted to ₹10,000 p.m. drawn at the beginning of each month.

The profits of the three years ending 31st March each year were; 2018 — Profit ₹1,20,000; 2019 — Loss ₹40,000; 2020 — Profit ₹1,90,000.

Profit of the firm from 1st April to 30th June, 2020 amounted to ₹30,000 before providing for salaries and interest.

Prepare *B*'s Current and Capital Accounts as they would appear in the books of the firm.

[**Ans.** Amount payable ₹2,11,800]

Hints : (1) Interest on *B*'s Drawings ₹300.

(2) As it is required to prepare *B*'s Current A/c, all items (except his capital) will be taken to his Current A/c and then the balance of his Current A/c will be transferred to the credit of his Capital A/c.

Q. 57. Following given is the Balance Sheet of Raghuvir and Co. in which *A*, *B* and *C* were partners sharing profits and losses in the ratio of 2 : 2 : 1 as at 31-3-2021:

BALANCE SHEET
as at 31-3-2021

Liabilities	₹	*Assets*	₹
Trade Creditors	76,000	Cash in Hand	54,000
Bills Payable	24,000	Debtors	82,000
Reserve Fund	28,000	Stock	52,000
Capitals :		Building	3,00,000
A	2,20,000	Investments	1,50,000
B	1,60,000		
C	1,30,000		
	6,38,000		6,38,000

B died on 30th September, 2021. His account has to be settled under the following terms :

(1) Goodwill is to be calculated at 3 year's purchase on the basis of average of last 3 years' profit or loss. The profits are :

The year ending on		₹
31-3-2019	Profit	37,000
31-3-2020	Profit	25,000
31-3-2021	(Loss)	8,000

(2) Profit for the period from 1-4-2021 to 30-9-2021 shall be ascertained proportionately on the basis of average profits and losses of the preceding 3 years.

(3) During 2020–21, a machinery costing ₹25,000 was purchased and debited to repairs account on which 25% depreciation is to be calculated.

(4) Other values agreed on assets are :

Stock	₹	60,000
Building	₹	3,20,000
Investments	₹	1,25,000

You are required to prepare Capital Accounts and Balance Sheet of the firm as at 30-9-2021 , transferring the amount due to *B* to his Executor's Account.

It is assumed that all other items of assets and liabilities remained the same.

[**Ans.** Adjusted Net Profit for the year ending on 31-3-2021 ₹10,750; Value of Goodwill ₹72,750; *B*'s share of Profit ₹4,850; Profit on revaluation ₹21,750; Balance transferred to *B*'s Executor's A/c ₹2,13,850. Capital Accounts : *A* ₹2,20,500 and *C* ₹1,30,250. B/S Total ₹6,64,600.]

Q. 58. Arun and Amit were partners sharing profits and losses in the ratio of 5 : 3 and their balance sheet as at 31st March, 2019 stood as under :

Liabilities	₹	*Assets*		₹
Capital A/cs :		Land on Leasehold		95,000
Arun	1,50,000	Plant and Machinery		50,000
Amit	75,000	Motor Van		20,000
Sundry Creditors	20,000	Stock in Hand		15,000
Bills Payable	5,000	Debtors	50,000	
		Less : Provision for Bad Debts	2,000	48,000
		Cash at Bank		22,000
	2,50,000			2,50,000

Amit died on 1st December, 2019 and the following decisions were taken :

(*a*) Goodwill to be calculated by taking thrice the amount of the average profit of the last four years. The profits of the previous years ending 31st March were: 2016 ₹15,000 (Profit); 2017 ₹20,000 (Profit); 2018 ₹10,000 (Loss); 2019 ₹35,000 (Profit).

(*b*) A provision of ₹5,000 is to be made in respect of outstanding legal charges.

(*c*) Further provision of ₹3,000 to be created on Debtors.

(*d*) Assets are to be revalued as following :

Leasehold Land	₹1,05,000
Plant & Machinery	₹ 65,000
Motor Van	₹ 18,000
Stock in Hand	₹ 12,000

(*e*) His share of profit for the period he was alive is to be based on the figure of profit on 31st March, 2019.

(*f*) Executor is entitled to Amit's Capital as appearing in the last balance sheet and interest thereon at 10% p.a. upto the date of death.

Prepare Revaluation Account, Partner's Capital Accounts and a Balance Sheet as at 1st December, 2019.

[**Ans.**

	₹
Profit on Revaluation	12,000
Amount transferred to Amits' executor's A/c	1,10,125
Balance of Arun's Capital A/c	1,40,625
P & L Suspense shown on the assets side (Share of Profit + Interest on Capital)	13,750
Balance Sheet Total	2,80,750]

Note : Amit's share of goodwill has been debited to Arun's Capital Account.

Q. 59. *M* and *N* were partners in a firm. Their profit sharing ratio was 3 : 2. On 31st March, 2020, their Balance Sheet stood as under :

Liabilities		₹	*Assets*	₹
Capital A/cs			Land and Building	6,00,000
M	5,00,000		Plant and Machinery	2,00,000
N	4,00,000	9,00,000	Furniture and Fixtures	90,000
General Reserve		60,000	Vehicles	75,000
Bank Overdraft		25,000	Goodwill	15,000
Sundry Creditors		75,000	Stock	30,000
			Debtors	50,000
		10,60,000		10,60,000

N died on 15th May, 2020. It was agreed that

(*a*) Land and Building to be appreciated to 120%.

(*b*) Value of Plant & Machinery, Furniture and Fixtures and Vehicles to be lowered by 10%.

(*c*) Goodwill to be valued at 3 years' purchase of last six years' average profits which were :

2014-15 ₹20,000; 2015-16 ₹18,000; 2016-17 ₹10,000;
2017-18 ₹ 7,000; 2018-19 ₹15,000; 2019-20 ₹20,000.

(*d*) ₹3,000 of Debtors proved bad and hence have to be written off and provision for ₹2,000 to be created on the Debtors.

(*e*) The profit for the year 2020-21 accrued on the same scale as in 2019-20.

(*f*) A sum of ₹68,400 to be paid immediately to the executor's of *N* and balance to be paid in 2 equal half-yearly instalments together with interest @ 7% per annum.

Pass the necessary journal entries to record the above transactions and prepare *N*'s Executor's account for the year 2020-21.

[**Ans.** Profit on Revaluation ₹78,500; Amount paid to *N*'s executors on 16th Nov. 2020 ₹2,14,000 (*i.e.*, instalment ₹2,00,000 + interest on ₹4,00,000 for six months); Balance left in *N*'s Executor's A/c ₹2,00,000.]

Q. 60. The following is the Balance Sheet of Ram, Mohan and Sohan as at 31st March, 2021 :

Liabilities	₹	*Assets*	₹
Sundry Creditors	10,000	Tools	3,000
Reserve Fund	7,500	Furniture	18,000
Capitals :		Stock	16,000
Ram	20,000	Debtors	12,000
Mohan	10,000	Cash at Bank	8,000
Sohan	10,000	Cash in Hand	500
	57,500		57,500

Ram, Mohan and Sohan shared profits and losses in the ratio of 2 : 2 : 1. Sohan died on 30th June, 2021. Under the partnership agreement the executor of Sohan was

entitled to :

(a) Amount standing to the credit of his Capital Account.

(b) Interest on Capital which amounted to ₹150.

(c) His share of goodwill ₹5,000.

(d) His share of profit from the closing of the last financial year to the date of death which amounted to ₹750.

Sohan's executor was paid ₹1,400 on 1st July, 2021 and the balance in four equal yearly instalments starting from 30th June, 2022 with interest @ 6% p.a.

Pass necessary Journal entries and draw up Sohan's Account to be rendered to his executor and Sohan's Executor's Account till it is finally paid.

[**Ans.** Balance of Sohan's Capital A/c transferred to his Executor's A/c ₹17,400; Annual instalment (excluding interest) ₹4,000. Interest allowed in four years ₹960; ₹720; ₹480 and ₹240 respectively; Amount paid in four years (inclusive of interest) ₹4,960; ₹4,720; ₹4,480 and ₹4,240 respectively.]

Q. 61. On 1st May, 2022, *A, B, C* and *D* were sharing profits and losses in the ratio of 1 : 2 : 3 : 4. *C* retires on this date and *A, B* and *D* agreed to share future profits and losses equally. On this date following balances appeared in their books :

	₹
Profit & Loss (Cr. Bal.)	80,000
Reserve Fund	40,000
Provident Fund	35,000

Partners decide to record the effect of retirement by a single journal entry. You are required to give the journal entry.

[**Ans.** *A*'s Capital A/c	Dr.	28,000	
B's Capital A/c	Dr.	16,000	
To *C*'s Capital A/c			36,000
To *D*'s Capital A/c			8,000]

Q. 62. *X, Y* and *Z* are partners sharing profits and losses in the ratio of 4 : 3 : 2. *Y* retires and *X* and *Z* decide to share future profits and losses in the ratio of 5 : 3. On the date of *Y*'s retirement, their Balance Sheet disclosed Dr. Balance of Profit & Loss A/c amounting to ₹2,70,000. Partners decide to record the effect of change in profit sharing ratio by a single journal entry. You are required to record the same.

[**Ans.** *Y*'s Capital A/c	Dr.	90,000	
To *X*'s Capital A/c			48,750
To *Z*'s Capital A/c			41,250]

Q. 63. *A, B* and *C* were partners sharing profits in the ratio of 1 : 3 : 2. Their fixed capitals were : *A* ₹3,00,000; *B* ₹4,00,000 and *C* ₹6,00,000. *A* retires and the new profit sharing ratio between *B* and *C* is agreed at 1 : 2. On this date, their Balance Sheet disclosed the following items :

BALANCE SHEET (an extract)

Liabilities	₹	*Assets*	₹
General Reserve	1,40,000	Advertisement Suspense Account	20,000
Profit and Loss Balance	30,000		

Partners decided to record the effect of the above items without affecting their book values. Pass the necessary adjusting entry.

[**Ans.**	C's Current A/c	Dr. 50,000	
	To A's Current A/c		25,000
	To B's Current A/c		25,000]

Q. 64. *A, B, C* and *D* are partners sharing profits in the ratio of 4 : 3 : 2 : 1. *A* retired on 1st May, 2022 and *B, C* and *D* decided to share future profits and losses equally. On this date their books show 'Workmen Compensation Reserve' of ₹1,20,000. Continuing partners do not want to alter the value of any item of Balance Sheet and want to record the effect of retirement by passing an adjustment entry. You are required to pass the adjustment entry under following alternative cases :

(*i*) When there is no claim for workmen compensation.

(*ii*) When claim for workmen compensation is estimated at ₹30,000

(*iii*) When claim for workmen compensation is estimated at ₹1,20,000

(*iv*) When claim for workmen compensation is estimated at ₹1,80,000

[**Ans.** Sacrifice Ratio : 1 : 4 : 7

(*i*) Dr. *B* ₹4,000, *C* ₹16,000, *D* ₹28,000 and Cr. *A* by ₹48,000.

(*ii*) Dr. *B* ₹3,000, *C* ₹12,000, *D* ₹21,000 and Cr. *A* by ₹36,000.

(*iii*) No Entry.

(*iv*) Dr. *A* ₹24,000 and Cr. *B* ₹2,000, *C* ₹8,000, *D* ₹14,000.]

Q. 65. *X, Y* and *Z* are partners sharing profits and losses in the ratio of 1 : 3 : 2. *X* retires on 1st April, 2022 and the new profit sharing ratio between *Y* and *Z* is agreed at 1 : 2. Following balances appeared in their Balance Sheet as at that date :

BALANCE SHEET *as at 1st April, 2022*

Liabilities	₹	*Assets*	₹
Investment Fluctuation Reserve	1,20,000	Investments (at cost)	6,00,000

Y and *Z* decide that book value of any item in the Balance Sheet is not to be altered but prefer to record the change in profit sharing ratio by an adjustment entry. Show the adjustment entry under the following alternative cases :

Case 1. If there is no other information
2. If the market value of investments is ₹5,52,000
3. If the market value of investments is ₹4,50,000
4. If the market value of investments is ₹6,30,000

[**Ans.** *Y* sacrifices 1/6; *Z* gains 2/6.

Case 1. *Z* Dr. ₹40,000; *X* and *Y* Cr. ₹20,000 each.
2. *Z* Dr. ₹24,000; *X* and *Y* Cr. ₹12,000 each.
3. *X* and *Y* Dr. ₹5,000 each and *Z* Cr. ₹10,000.
4. *Z* Dr. ₹50,000; *X* and *Y* Cr. ₹25,000 each.]

Q. 66. The Balance Sheet of *P, Q* and *R* who were sharing profits and losses in the ratio of $\frac{1}{2} : \frac{1}{3} : \frac{1}{6}$ respectively stood as follows as at 31st March 2022 :

Liabilities		₹	Assets	₹
Creditors		1,30,000	Land and Building	10,00,000
General Reserve		2,70,000	Investments	
Workmen Compensation Reserve		60,000	(Market Value ₹2,00,000)	2,50,000
Investment Fluctuation Reserve		20,000	Stock	2,00,000
Capitals :			Debtors	1,50,000
P	6,00,000		Cash at Bank	1,20,000
Q	4,00,000		Advertisement Suspense	60,000
R	3,00,000	13,00,000		
		17,80,000		17,80,000

Q retires and *P* and *R* decide to share future profits and losses in the ratio of 3 : 2. Claim on account of Workmen Compensation is estimated at ₹45,000. *P* and *R* agreed that effect of retirement is to be recorded by a single journal entry.

Also prepare the Capital Accounts of partners.

[**Ans.** Gaining Ratio 3 : 7. Balance of Capital Accounts *P* ₹5,80,500 and *R* ₹2,54,500. Amount due to *Q* ₹4,65,000.]

Q. 67. *A*, *B* and *C* are partners sharing profits and losses in the ratio of 2 : 3 : 1. Their Balance Sheet as at 31st March 2022 is given below :

Liabilities		₹	Assets		₹
Creditors		2,00,000	Bank		3,37,000
Profit & Loss Account		1,20,000	Debtors	4,00,000	
General Reserve		1,50,000	*Less :* Provision for		
Workmen Compensation Reserve		80,000	Doubtful		
Investment Fluctuation Reserve		50,000	Debts	25,000	3,75,000
Capital A/cs :			Stock		5,10,000
A	6,00,000		Investments		
B	7,00,000		(Market Value ₹1,32,000)		1,50,000
C	3,00,000	16,00,000	Land & Building		8,00,000
			Advertisement Expenditure		28,000
		22,00,000			22,00,000

C retires on 1st April, 2022 and *A* and *B* continued in partnership, sharing future profits and losses in the ratio of 3 : 2. Following was agreed upon :

(*i*) Land & Building is to be appreciated by 10% and Stock was found overvalued by ₹20,000.

(*ii*) Provision for Doubtful Debts is to be made equal to 5% of the debtors.

(*iii*) Claim on account of Workmen Compensation is ₹24,000.

(*iv*) Goodwill of the firm be valued at ₹4,50,000.

(*v*) A debtor whose due of ₹20,000 was written off as bad debts paid 50% in full settlement.

(*vi*) *A* and *B* decide that after the adjustment of Workmen Compensation Claim from Workmen Compensation Reserve and difference between market value

and book value of investments from Investment Fluctuation Reserve, remaining balance of such reserves and all accumulated profits/losses are to appear in the Balance Sheet of the new firm.

(vii) Amount due to C is to be settled 50% on retirement and balance 50% within one year.

Prepare Revaluation Account, Partner's Capital Accounts and the Balance Sheet after C's retirement.

[**Ans.** Profit on Revaluation ₹75,000; C's Loan A/c ₹2,21,250; Capital A/cs A ₹4,17,000 and B ₹8,15,500; B/S Total ₹20,35,750.]

Hints : (i) A gains $\frac{8}{30}$; B Sacrifices $\frac{3}{30}$ and C Sacrifices $\frac{5}{30}$.

(ii) Adjustment Journal Entry for Accumulated Profits and Losses :

A's Capital A/c ($3,30,000 \times \frac{8}{30}$)	Dr.	88,000	
To B's Capital A/c ($3,30,000 \times \frac{3}{30}$)			33,000
To C's Capital A/c ($3,30,000 \times \frac{5}{30}$)			55,000

Q. 68. The Balance Sheet of A, B and C who were sharing profits in the ratio of 5 : 3 : 2 as at 31st March 2022 was as under :

Liabilities	₹	*Assets*		₹
Sundry Creditors	1,50,000	Cash at Bank		1,20,000
General Reserve	2,45,000	Sundry Debtors	3,00,000	
Workmen Compensation Reserve	60,000	*Less :* Provision for Doubtful Debts	15,000	2,85,000
Investment Fluctuation Reserve	45,000	Stock		1,25,000
A's Capital	4,50,000	Investments (Market Value ₹2,40,000)		2,00,000
B's Capital	3,00,000	Land & Building		6,80,000
C's Capital	2,50,000	Goodwill		50,000
		Advertisement Suspense		40,000
	15,00,000			15,00,000

A retired on 1st April, 2022 and B and C decided to share future profits and losses in the ratio of 2 : 3. The partners agreed to the following terms :

(i) Goodwill of the firm is valued at ₹2,00,000.

(ii) Land and Building is undervalued by ₹1,20,000.

(iii) There were bad debts ₹25,000.

(iv) A provision for ₹20,000 is to be made for outstanding legal charges.

(v) A claim of ₹40,000 on account of Workmen Compensation is to be provided.

(vi) Continuing partners decided to record the effect of reserves (after adjusting claim on account of Workmen Compensation Reserve) and accumulated profits/losses without affecting their book values.

(vii) The amount to be paid to A is to be brought in by B and C in such a way that their Capitals are proportionate to their profit sharing ratio and leave a balance of ₹50,000 in the Bank Account.

Prepare Revaluation Account, Partner's Capital Accounts and the Balance sheet of the new firm.

[**Ans.** Profit on Revaluation ₹1,30,000; Amount paid to A ₹7,25,000; Final Capitals B ₹4,04,000 and C ₹6,06,000; B brings in ₹1,27,000 and C brings in ₹5,28,000; B/S Total 15,30,000.]

Hints : (i) Gaining Ratio 1 : 4

(ii) Adjustment Journal Entry for Accumulated Profits and Losses :

B's Capital A/c ($\frac{1}{5}$ of ₹1,35,000)	Dr.	27,000	
C's Capital A/c ($\frac{4}{5}$ of ₹1,35,000)	Dr.	1,08,000	
To A's Capital A/c ($\frac{5}{10}$ of ₹2,70,000)			1,35,000

ADDITIONAL QUESTIONS

Q. 69. Ravi, Mukesh, Naresh and Yogesh are partners in a firm sharing profits in the ratio of 2 : 2 : 1 : 1. On Mukesh's retirement the goodwill of the firm is valued at ₹90,000. Ravi, Naresh and Yogesh decided to share future profits equally. Pass the necessary journal entry for the treatment of goodwill.

[**Ans.** Naresh's Capital A/c	Dr.	15,000	
Yogesh's Capital A/c	Dr.	15,000	
To Mukesh's Capital A/c			30,000]

Q. 70. A, B and C are partners sharing profits in the ratio of 4 : 3 : 3. On C's retirement the value of the firm's Goodwill was agreed at ₹3,00,000. A and B agreed to share profits and losses in future in the ratio of 7 : 3. Give adjustment entry in relation to goodwill.

[**Ans.** A's Capital A/c	Dr.	90,000	
To C's Capital A/c			90,000]

Q. 71. L, M and O were partners in a firm sharing profits in 1 : 3 : 2 ratio. L retired and the new profit sharing ratio between M and O was 1 : 2. On L's retirement the goodwill of the firm was valued at ₹1,20,000. Pass necessary journal entry for the treatment of goodwill on L's retirement.

[**Ans.** O's Capital A/c(1,20,000 × 2/6)	Dr.	40,000	
To L's Capital A/c (1,20,000 × 1/6)			20,000
To M's Capital A/c (1,20,000 × 1/6)			20,000]

Working Notes : O Gains $= \frac{2}{3} - \frac{2}{6} = \frac{2}{6}$

M Sacrifice $= \frac{1}{3} - \frac{3}{6} = \frac{1}{6}$

Q. 72. X, Y and Z are in partnership sharing profits in the proportion of 3 : 2 : 1. There is no goodwill A/c in the books of the firm.

As from 1st April, 2020, it was agreed that *X* should give only part of time, to the business and that in consequence he should receive in future only one half of his previous share, the remaining half being divided equally between *Y* and *Z*. The goodwill to be valued for this purpose, at ₹40,000.

Show the new share of partners and pass necessary journal entry.

[**Ans.** New Profit sharing ratio of *X*, *Y* and *Z* will be 6 : 11 : 7 respectively.

Entry will be :

Y's Capital A/c	Dr.	5,000	
Z's Capital A/c	Dr.	5,000	
To *X*'s Capital A/c			10,000]

Q. 73. Krish, Vrish and Peter are partners sharing profits in the ratio of 3 : 2 : 1. Vrish retired from the firm. On that date the Balance Sheet of the firm was as follows :

BALANCE SHEET
as at 31st March, 2020

Liabilities	₹	*Assets*		₹
Creditors	15,000	Bank		7,600
General Reserve	12,000	Furniture		41,000
Bills Payable	12,000	Stock		9,000
Outstanding Salary	2,200	Premises		80,000
Provision for Legal Damages	6,000	Debtors	6,000	
Capitals :		*Less* : Provision for		
Krish	46,000	Doubtful Debts	400	5,600
Vrish	30,000			
Peter	20,000			
	1,43,200			1,43,200

Additional Information :

(*i*) Premises to be appreciated by 20%, Stock to be depreciated by 10% and Provision for doubtful debts was to be maintained @ 5% on Debtors. Further, provision for legal damages is to be increased by 1,200 and furniture to be brought up to ₹45,000.

(*ii*) Goodwill of the firm is valued at ₹42,000.

(*iii*) ₹26,000 from Vrish's Capital Account be transferred to his loan account and balance to be paid through bank; if required, necessary loan may be obtained from bank.

(*iv*) New profit sharing ratio of Krish and Peter is decided to be 5 : 1.

Prepare Revaluation Account, Partners Capital Accounts and Balance Sheet.

(C.B.S.E. Sample Paper, 2020)

[**Ans.** Profit on Revaluation ₹18,000; Net amount paid to Vrish ₹28,000; Balance of Capital A/cs : Krish ₹47,000 and Peter ₹25,000; Balance Sheet Total ₹1,54,800.]

Q. 74. Kavya, Manya and Navita were partners sharing profits as 50%, 30% and 20% respectively. On 31-3-2016, their Balance Sheet was as under :

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Creditors		1,40,000	Fixed Assets		8,90,000
General Reserve		1,00,000	Investments		2,00,000
Capitals :			Stock		1,30,000
Kavya	6,00,000		Debtors	4,00,000	
Manya	5,00,000		*Less* : Provision for		
Navita	4,00,000	15,00,000	Bad Debts	30,000	3,70,000
			Bank		1,50,000
		17,40,000			17,40,000

On the above date, Kavya retired and Manya and Navita agreed to continue the business on the following terms :

(*a*) Firm's goodwill was valued at ₹60,000 and it was decided to adjust Kavya's share of goodwill in the capital accounts of continuing partners.

(*b*) There was a claim for workmen's compensation to the extent of ₹4,000.

(*c*) Investments were revalued at ₹2,13,000.

(*d*) Fixed Assets were to be depreciated by 10%.

(*e*) Kavya was to be paid ₹20,000 through a bank draft and the balance was transferred to her loan account which will be paid in two equal annual instalments together with interest @10% p.a.

Prepare Revaluation A/c, Partner's Capital accounts and Kavya's Loan Account till it is finally paid. *(C.B.S.E. 2018, Comptt.)*

[**Ans.** Loss on Revaluation ₹80,000; Kavya's Loan ₹6,20,000; Capital A/cs : Manya ₹4,88,000 and Navita ₹3,92,000.
Amount paid on 31st March 2017 : ₹3,10,000 + Interest ₹62,000
Amount paid on 31st March 2018 : ₹3,10,000 + Interest ₹31,000]

Q. 75. Kanika, Disha and Kabir were partners sharing profits in the ratio 2 : 1 : 1. On 31-3-2016, their Balance Sheet was as under :

Liabilities	*Amount*	*Assets*	*Amount*
	₹		₹
Trade creditors	53,000	Bank	60,000
Employees Provident Fund	47,000	Debtors	60,000
Kanika's Capital	2,00,000	Stock	1,00,000
Disha's Capital	1,00,000	Fixed Assets	2,40,000
Kabir's Capital	80,000	Profit & Loss A/c	20,000
	4,80,000		4,80,000

Kanika retired on 1-4-2016. For this purpose, the following adjustments were agreed upon:

(a) Goodwill of the firm was valued at 2 years' purchase of average profits of three completed years preceding the date of retirement. The profits for the year :
2013-14 were ₹1,00,000 and for 2014-15 were ₹1,30,000.

(b) Fixed assets were to be increased to ₹3,00,000.

(c) Stock was to be valued at 120%.

(d) The amount payable to Kanika was transferred to her loan account.

Prepare Revaluation Account, Capital Accounts of the partners and the Balance Sheet of the reconstituted firm. *(C.B.S.E. 2017 Comptt.)*

[**Ans.** Profit on Revaluation ₹80,000; Kanika's Loan A/c ₹3,00,000; Capital A/cs Disha ₹80,000 and Kabir ₹60,000; B/S Total ₹5,40,000.]

Hint. Kanika's share of goodwill ₹70,000.

Q. 76. *A, B* and *C* were in partnership sharing profits in proportion to their capitals. Their Balance Sheet as at 31-3-2018 was as follows :

Liabilities	₹	*Assets*		₹
Creditors	15,600	Cash		16,000
Reserve	6,000	Debtors	20,000	
A's Capital	90,000	*Less* : Provision for		
B's Capital	60,000	Doubtful Debts	400	19,600
C's Capital	30,000	Stock		18,000
		Machinery		48,000
		Buildings		1,00,000
	2,01,600			2,01,600

On the above date *B* retired owing to ill health and the following adjustments were agreed upon :

(a) Buildings be appreciated by 10%.

(b) Provision for bad and doubtful debts be increased to 5% on debtors.

(c) Machinery be depreciated by 15%.

(d) Goodwill of the firm be valued at ₹36,000 and be adjusted into the Capital Accounts of *A* and *C* who will share profits in future in the ratio of 3 : 1.

(e) A provision be made for outstanding repairs bill of ₹3,000.

(f) Included in the value of creditors is ₹1,800 for an outstanding legal claim, which is not likely to arise.

(g) Out of the insurance premium paid ₹2,000 is for the next year. The amount was debited to P & L A/c.

(h) The partners decide to fix the capital of the new firm as ₹1,20,000 in the profit sharing ratio.

(i) *B* to be paid ₹9,000 in cash and the balance to be transferred to his Loan Account.

Prepare the Revaluation Account, Partner's Capital Accounts and the Balance Sheet of the new firm after *B*'s retirement. *(C.B.S.E. Sample Paper, 2020)*

[**Ans.** Profit on Revaluation ₹3,000; Capital Accounts *A* ₹90,000 and *C* ₹30,000;

Deficit Capital brought in by *A* ₹4,500 and *C* ₹1,500; Cash Balance ₹13,000; B/S Total ₹2,02,800.]

Q. 77. Mohan, Vinay and Nitya were partners in a firm sharing profits and losses in the proportion of $\frac{1}{2}$, $\frac{1}{3}$ and $\frac{1}{6}$ respectively. On 31st March, 2018, their Balance Sheet was as follows :

Liabilities		₹	*Assets*		₹
Creditors		48,000	Cash at Bank		31,000
Employees' Provident Fund		1,70,000	Bills Receivable		54,000
Contingency Reserve		30,000	Book Debts	63,000	
Capitals :			*Less* : Provision for		
Mohan	1,20,000		Doubtful Debts	2,000	61,000
Vinay	1,00,000		Plant and Machinery		1,20,000
Nitya	90,000	3,10,000	Land and Building		2,92,000
		5,58,000			5,58,000

Mohan retired on the above date and it was agreed that :

(*i*) Plant and Machinery will be depreciated by 5%.

(*ii*) An old computer previously written off was sold for ₹4,000.

(*iii*) Bad debts amounting to ₹3,000 will be written off and a provision of 5% on debtors for bad and doubtful debts will be maintained.

(*iv*) Goodwill of the firm was valued at ₹1,80,000 and Mohan's share of the same was credited in his account by debiting Vinay's and Nitya's accounts.

(*v*) The capital of the new firm was to be fixed at ₹90,000 and necessary adjustments were to be made by bringing in or paying off cash as the case may be.

(*vi*) Vinay and Nitya will share future profits in the ratio of 3 : 2.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet of the reconstituted firm. *(C.B.S.E. 2019, Rajasthan)*

[**Ans.** Loss on Revaluation ₹6,000; Mohan's Loan A/c ₹2,22,000; Capital Accounts : Vinay ₹54,000 and Nitya ₹36,000; Amount returned to Vinay ₹6,000 and to Nitya ₹16,000; B/S Total ₹5,30,000.]

Hints : (1) Entry for Computer Sold :

Bank A/c	Dr. 4,000	
To Revaluation A/c		4,000
(2) (*i*) Bad Debts A/c	Dr. 3,000	
To Book Debts (Debtors)		3,000
(*ii*) Provision for Doubtful Debts A/c	Dr. 2,000	
Revaluation A/c (3,000 – 2,000)	Dr. 1,000	
To Bad Debts A/c		3,000
(*iii*) Revaluation A/c	Dr. 3,000	
To Provision for Doubtful Debts A/c		3,000

Q. 78. *A*, *B* and *C* are partners sharing profits in the ratio of their Capitals. Their Balance Sheet as at March 31, 2022 is as under :

Liabilities		₹	*Assets*	₹
Capitals :			Bank	44,800
A	2,00,000		Sundry Debtors	1,72,000
B	2,00,000		Stock	3,00,000
C	1,00,000	5,00,000	Furniture and Fittings	46,000
Reserve Fund		40,000		
Sundry Creditors		20,000		
Outstanding Expenses		2,800		
		5,62,800		5,62,800

A retired on this date.

Additional Information :

(*i*) Furniture and fittings were undervalued by ₹4,000.

(*ii*) An amount of ₹12,000 due from Mr. Arun, a debtor, was doubtful and a provision for the same is required.

(*iii*) Stock be valued at 90%.

(*iv*) Goodwill of the firm be valued at ₹60,000.

(*v*) ₹1,00,000 be transferred to *A*'s loan account and balance be paid through bank. Bank overdraft be arranged, if required.

(*vi*) *B* and *C* will share future profits in 5 : 3.

Prepare necessary ledger accounts and balance sheet of the firm after *A*'s retirement.

[**Ans.** Loss on Revaluation ₹38,000; Amount paid to *A* ₹1,24,800. Bank Overdraft ₹80,000; Capital Accounts *B* ₹1,87,300 and *C* ₹89,900. Balance Sheet Total ₹4,80,000. Gaining Ratio 9 : 7.]

Q. 79. Following is the Balance Sheet of *G*, *K* & *W* as at 31st March, 2022 who share profits in the ratio of 3 : 2 : 1.

Liabilities		₹	*Assets*	₹
Capital Accounts :			Goodwill	7,500
G	22,000		Stock	12,500
K	13,000		Sundry Debtors	12,000
W	9,000	44,000	Land and Buildings	15,000
Sundry Creditors		10,000	Plant and Machinery	18,000
Bills Payable		4,000	Motor Vehicle	5,000
General Reserve		12,000		
		70,000		70,000

On 1st April, 2022, *G* retired and the following arrangements were agreed upon :

(1) Goodwill of the firm is to be valued at ₹15,000.

(2) The assets and liabilities are to be valued as under : Stock ₹10,000; Sundry Debtors ₹11,500; Land and Buildings ₹18,000; Plant and Machinery ₹16,500; and Sundry Creditors ₹9,200.

(3) Liability for Workmen's Compensation amounting to ₹500 is to be brought into the books.

(4) *K* and *W* were to introduce ₹12,000 and ₹6,000 respectively into the business and ₹13,150 were paid to *G*. The balance due to him was to be paid in three equal instalments annually together with interest @ 12% per annum.

Give necessary ledger accounts, the Balance Sheet of the firm after *G*'s retirement and *G*'s Loan Account till it is finally paid off.

[**Ans.** Loss on Revaluation ₹1,200; Balance of *G*'s Loan A/c on 1st April, 2022 ₹18,000; Capital Accounts : *K* ₹21,100 and *W* ₹13,050; Cash Balance 4,850; B/S Total ₹65,850]

Q. 80. The Balance Sheet of Messrs *A*, *B* and *C* showed as follows :

Liabilities		₹	*Assets*		₹
Trade Creditors		7,000	Freehold Property		49,000
Capital Accounts :			Plant		15,000
A	22,575		Stock		5,500
B	30,000		Sundry Debtors	6,250	
C	18,500	71,075	*Less* : Bad Debt Provision	100	6,150
			Cash at Bank		2,425
		78,075			78,075

B agrees to take over the business, *A* and *C* retiring on the following terms :

(*a*) That the goodwill of the firm be valued at ₹15,000

(*b*) That plant and stock be reduced by 10%.

(*c*) That freehold property be appreciated by ₹1,000.

(*d*) That Provision for doubtful debts be brought up to ₹250.

(*e*) *B* has to bring in sufficient cash to pay off *A* and *C*. The partners used to share profits in the proportion of 2/5, 2/5 and 1/5.

Show the necessary Journal entries, Partner's Capital Accounts and Balance Sheet of *B* after the retirement of *A* and *C*.

[**Ans.** Loss on Revaluation ₹1,200; *A* and *C* were paid ₹28,095 and ₹21,260 respectively; *B* brought Cash ₹46,930; *B*'s Capital ₹67,450; B/S Total ₹74,450]

Hint : *A* and *C*'s share of goodwill will be debited to *B*'s account.

Q. 81. *A*, *B* and *C* are partners sharing profits and losses in the ratio of 3/6 : 2/6 : 1/6. Following is their Balance Sheet as at 31st March, 2022 :

Liabilities		₹	*Assets*	₹
Creditors		52,000	Plant	2,50,000
Outstanding Expenses		10,000	Stock	1,50,000
Capitals :			Debtors	80,000
A	2,00,000		Bank	70,000

B	1,60,000		Profit & Loss A/c	12,000
C	1,40,000	5,00,000		
		5,62,000		5,62,000

B retires on 1st April, 2022 and the following terms were agreed :

(*i*) The Goodwill of the firm has been valued at ₹1,50,000.

(*ii*) Plant and Machinery has been revalued at ₹3,00,000 and stock revalued at ₹1,20,000.

(*iii*) A sum of ₹30,000 out of debtors was agreed to be bad and was to be written off.

(*iv*) Liability for workmen's compensation to the extent of ₹8,000 is to be brought into the books.

(*v*) *A* and *C* will continue to carry on the business and shall share profits and losses equally in future.

(*vi*) Amount payable to *B* shall remain in the business as loan carrying interest at 18% p.a.

You are required to :

(*a*) give journal entries to give effect to the above, and

(*b*) prepare the opening balance sheet of *A* and *B* at 1st April, 2022.

[**Ans.** Loss on Revaluation ₹18,000; *C* gains 2/6 and would be debited for goodwill alone. Balances of Capital A/cs : *A* ₹1,85,000 and *C* ₹85,000; *B*'s Loan A/c ₹2,00,000; B/S Total ₹5,40,000]

Q. 82. Akul, Bakul and Chandan were partners in a firm sharing profits in the ratio of 2 : 2 : 1. On 31st March, 2018 their Balance Sheet was as follows :

BALANCE SHEET OF AKUL, BAKUL AND CHANDAN

as at 31-3-2018

Liabilities		₹	*Assets*		₹
Sundry Creditors		45,000	Cash at Bank		42,000
Employees Provident Fund		13,000	Debtors	60,000	
General Reserve		20,000	*Less* : Provision for		
Capitals :			Doubtful Debts	2,000	58,000
Akul	1,60,000		Stock		80,000
Bakul	1,20,000		Furniture		90,000
Chandan	92,000	3,72,000	Plant and Machinery		1,80,000
		4,50,000			4,50,000

Bakul retired on the above date and it was agreed that :

(*i*) Plant and Machinery was undervalued by 10%.

(*ii*) Provision for doubtful debts was to be increased to 15% on debtors.

(*iii*) Furniture was to be decreased to ₹87,000.

(*iv*) Goodwill of the firm was valued at ₹3,00,000 and Bakul's share was to be adjusted through the capital accounts of Akul and Chandan.

(v) Capital of the new firm was to be in the new profit sharing ratio of the continuing partners (actual cash to be brought in or paid off, as the case may be.)

Prepare Revaluation account, Partners' Capital accounts and the Balance Sheet of the reconstituted firm. *(C.B.S.E. 2019, M.P.)*

[**Ans.** Profit on Revaluation ₹10,000; Bakul's Loan ₹2,52,000; Capital Accounts Akul ₹1,00,000 and Chandan ₹50,000; Cash brought in by Akul ₹8,000 and withdrawn by Chandan ₹8,000; Balance Sheet Total ₹4,60,000.]

Q. 83. *G, E* and *F* were partners in a firm sharing profits in the ratio of 7 : 2 : 1. The Balance Sheet of the firm as at 31st March, 2018, was as follows :

BALANCE SHEET OF *G, E* AND *F*

as at 31st March, 2018

Liabilities		₹	*Assets*	₹
Capitals :			Cash	90,000
G	1,40,000		Sundry Debtors	24,000
E	40,000		Stock	14,000
F	20,000	2,00,000	Machinery	80,000
Creditors		28,000	Land and Building	1,20,000
General Reserve		40,000		
Loan from *E*		60,000		
		3,28,000		3,28,000

E retired on the above data. On *E*'s retirement the following was agreed upon :

(*i*) Land and Building were revalued at ₹1,88,000, Machinery at ₹76,000 and Stock at ₹10,000 and goodwill of the firm was valued at ₹90,000.

(*ii*) A provision of 2.5% was to be created on sundry debtors for doubtful debts.

(*iii*) The net amount payable to *E* was transferred to his loan account to be paid later on.

(*iv*) Total capital of the new firm was fixed at ₹2,40,000 which will be adjusted according to their new profit sharing ratio by opening current accounts.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet of reconstituted firm. *(C.B.S.E. 2019, Kerala)*

[**Ans.** Profit on Revaluation ₹59,400; *E*'s loan ₹1,37,880; Capital Accounts *G* ₹2,10,000 and *F* ₹30,000; *G*'s Current A/c (Dr.) ₹16,170; *F*'s Current A/c (Dr.) ₹2,310; Balance Sheet Total ₹4,05,880.]

Q. 84. *A, B* and *C* were partners sharing profits and losses in the ratio of 3 : 2 : 1. Their Balance Sheet as at 31-03-2022 stood as follows :

Liabilities		₹	*Assets*		₹
Sundry Creditors		12,500	Cash at Bank		1,500
General Reserve		18,000	Sundry Debtors	15,000	
Capital A/cs :			*Less* : Provision for Bad		
A	40,000		Debts	1,500	13,500

B	21,000		Stock	20,500
C	20,000	81,000	Office Equipments	14,000
			Furniture	12,000
			Building	50,000
		1,11,500		1,11,500

B retired on 1-4-2022 subject to the following conditions :

(*i*) A typewriter purchased on 1-10-2021 for ₹2,000 debited to office expenses account is to be brought into account charging depreciation @ 10% p.a.

(*ii*) Building revalued at ₹75,000. Furniture is to be written-down by ₹2,000 and stock is reduced to ₹17,500.

(*iii*) Provision for bad debts is to be calculated @ 5% on debtors.

(*iv*) Goodwill of the firm is to be valued at ₹18,000.

(*v*) Amount due to *B* is to be transferred to his Loan Account.

(*vi*) *A* and *C* will share profits and losses in the ratio of 2 : 1 and their capitals are to be adjusted in the profit sharing ratio.

You are required to prepare : Revaluation Account, Partners' Capital Accounts and Balance Sheet immediately after *B*'s retirement.

[**Ans.** Profit on Revaluation ₹22,650; *B*'s Loan A/c ₹40,550; Final balance of Capital Accounts *A* ₹54,067 and *C* ₹27,033; *A* withdraws ₹3,258 and *C* brings in ₹3,258; Balance Sheet Total ₹1,34,150.]

Q. 85. *A*, *B* and *C* were in partnership sharing profits and losses in the ratio of 3 : 2 : 1. Their Balance Sheet as at 31st March, 2022 was as follows :

Liabilities		₹	*Assets*		₹
Capital Accounts :			Plant & Machinery		30,000
A	18,000		Furniture		15,000
B	16,000		Trade Debtors	35,000	
C	10,000	44,000	*Less* : Provision	2,000	33,000
Trade Creditors		33,000	Cash in Hand		1,000
Workmen's Accident Compensation Reserve		5,000	Profit & Loss A/c		3,000
		82,000			82,000

C retired on this date. It was agreed that :

(*i*) Plant and Machinery is to be revalued at ₹40,000; the existing provision for bad debts is to be increased by 50% and liability for workmen's compensation was decided at ₹2,000.

(*ii*) Creditors are to be paid ₹3,000 more.

(*iii*) *C*'s share of goodwill was valued at ₹8,000.

(*iv*) The total amount payable to *C* was brought in by *A* and *B* in such a way as to make their capital accounts in proportion to their share of profits which is to be equal.

You are required to prepare (*i*) revaluation account, (*ii*) partners' capital accounts, and (*iii*) revised balance sheet after all adjustments are carried out.

[**Ans.** Profit on Revaluation ₹6,000; Amount paid to *C* ₹19,000; Capital Accounts *A* ₹25,000; *B* ₹25,000; B/S Total ₹88,000; Cash balance ₹1,000; Cash brought in by *A* ₹4,000 and by *B* ₹15,000.]

Hint : 'Liability for Workmen's Accident Compensation' amounting to ₹2,000 will be shown on the liabilities side of the new balance sheet and the balance of ₹3,000 will be distributed among all the partners.

Q. 86. Radha, Manas and Arnav were partners in a firm sharing profits and losses in the ratio of 3 : 1 : 1. Their Balance Sheet as at 31st March, 2019 was as follows:

BALANCE SHEET OF RADHA, MANAS AND ARNAV
as at 31st March, 2019

Liabilities		₹	*Assets*		₹
Capitals :			Furniture		4,60,000
Radha	4,00,000		Investments		2,00,000
Manas	3,00,000		Stock		2,40,000
Arnav	2,00,000	9,00,000	Sundry Debtors	2,20,000	
Investment Fluctuation Fund		1,10,000	*Less* : Provision for		
Creditors		2,50,000	Doubtful Debts	10,000	2,10,000
			Cash		1,50,000
		12,60,000			12,60,000

Manas retired on 1st April, 2019. It was agreed that :

(*i*) Stock was to be appreciated by 20%.

(*ii*) Provision for doubtful debts was to be increased to ₹15,000.

(*iii*) Value of furniture was to be reduced by ₹3,000.

(*iv*) Market value of investments was ₹1,90,000.

(*v*) Goodwill of the firm was valued at ₹2,00,000 and Manas's share was adjusted in the accounts of Radha and Arnav.

(*vi*) Manas was paid ₹68,000 in cash and the balance was transferred to his loan account.

(*vii*) Capitals of Radha and Arnav were to be in proportion to their new profit sharing ratio. Surplus/deficit, if any, in their capital accounts was to be adjusted through current accounts.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet of the reconstituted firm. *(C.B.S.E. 2020, Rajasthan)*

[**Ans.** Profit on Revaluation ₹40,000; Manas Loan A/c₹3,00,000; Capital A/cs : Radha ₹5,04,000 and Arnav ₹1,68,000; Current A/cs : Radha ₹50,000 (Dr.), Arnav ₹50,000 (Cr.); Balance Sheet Total ₹12,72,000.]

Q. 87. *A*, *B* and *C* are partners sharing profits and losses in the ratio of 5 : 3 : 2. Their Balance Sheet as at 31st March, 2022 was as follows :

Liabilities		₹	Assets	₹
Sundry Creditors		29,000	Goodwill	24,000
Provision for Doubtful Debts		5,000	Debtors	80,000
Capitals :			Investments	30,000
A	1,40,000		Land & Building	1,42,000
B	90,000		Machinery	50,000
C	76,000	3,06,000	Patents	4,000
			Cash at Bank	10,000
		3,40,000		3,40,000

C retired on 1st April, 2022 as per the following conditions :

(*i*) Goodwill of the firm is to be valued at three years purchase of the average profits of the last five years which were ₹20,000; ₹12,000; ₹30,000; ₹6,000 (loss) and ₹34,000 respectively.

(*ii*) Machinery is to be reduced to ₹40,000 and patents are valueless.

(*iii*) There is no need of any provision for doubtful debts.

(*iv*) An unclaimed liability of ₹2,000 is to be written off.

(*v*) Out of the total insurance premium paid, ₹1,000 be treated as pre-paid.

(*vi*) Investments are revalued at ₹16,000 and these are taken by *C* at this value.

Entire sum payable to *C* is to be brought in by *A* and *B* in such a way so as to make their capitals proportionate to their new profit sharing ratio which is 2 : 1.

Prepare Revaluation Account, Capital Accounts and the opening Balance Sheet of *A* and *B*.

[**Ans.** Loss on Revaluation ₹20,000; Amount paid to *C* ₹62,000; Final Balances of Capital Accounts *A* ₹1,64,000 and *B* ₹82,000; Cash brought in by *A* ₹55,000 and by *B* ₹7,000; B/S Total ₹2,73,000]

Q. 88. *A, B* and *C* were equal partners. Their Balance Sheet as at 31-3-2022 was as under :

BALANCE SHEET *as at 31-3-2022*

Liabilities		₹	Assets		₹
B/P		20,000	Bank		20,000
Creditors		40,000	Stock		20,000
General Reserve		30,000	Furniture		28,000
P/L		6,000	Debtors	45,000	
Capitals :			*Less* : RBDD	5,000	40,000
A	60,000		Land & Building		1,20,000
B	40,000				
C	32,000	1,32,000			
		2,28,000			2,28,000

B retired on 1st April, 2022. *A* and *C* decided to continue the business as equal partners on the following terms :

(a) Goodwill of the firm was valued at ₹57,600.
(b) Reserve for bad and doubtful debts to be maintained at 10% on debtors.
(c) Land and building to be increased to ₹1,32,000.
(d) Furniture to be reduced by ₹8,000.
(e) Rent outstanding (not provided for as yet) was ₹1,500.

Remaining partners decided to bring sufficient cash in the business to pay off B and to maintain a bank balance of ₹24,800. They also decided to readjust their capitals as per their new profit sharing ratio.

Prepare necessary Ledger Accounts and Balance Sheet.

[**Ans.** Profit on Revaluation : ₹3,000; Cash paid to B ₹72,200; Final Capitals ₹87,900 each; A brings in ₹24,500 and C brings in ₹52,500; B/S Total ₹2,37,300.]

Q. 89. X, Y and Z are partners sharing profits and losses in the ratio of 3 : 2 : 1. Their Balance Sheet as at 31st March, 2022 was as follows :

Liabilities		₹	*Assets*		₹
Sundry Creditors		51,000	Buildings		2,00,000
Employees Provident Fund		9,000	Machinery		80,000
Capitals :			Sundry Debtors	1,00,000	
X	1,52,000		*Less* : Provision	10,000	90,000
Y	1,48,000		Stock		40,000
Z	84,000	3,84,000	Cash at Bank		22,000
			Profit & Loss A/c		12,000
		4,44,000			4,44,000

X retired on that date and it was decided to make the following adjustments :

(i) Stock to be depreciated by 40% and sale of old papers and materials realised ₹1,000.
(ii) Provision for doubtful debts to be increased to 17% of Sundry Debtors.
(iii) Machinery be depreciated by 40% and buildings be appreciated by 20%.
(iv) Partners paid ₹10,000 to the family of an employee who died of an heart-attack.
(v) Goodwill is valued at ₹30,000.
(vi) Y and Z decided to share future profits in the ratio of 3 : 2 and not to show goodwill in the books.
(vii) Y and Z would introduce sufficient capital to pay off X and have thereafter a sum of ₹25,000 as Working Capital in a manner that their Capitals would be in proportion of their new profit sharing ratio.

Pass journal entries and prepare the Balance Sheet of the new firm.

[**Ans.** Loss on Revaluation ₹24,000; Cash paid to X ₹1,49,000; Final Capitals Y ₹2,16,000; Z ₹1,44,000; Y brings in ₹88,000 and Z brings in ₹73,000; B/S Total ₹4,20,000]

Hints : (I) Entry for sale of old papers and materials :

Bank A/c	Dr.	1,000	
To Revaluation A/c			1,000

(II) Entry for payment of ₹10,000 to the family of ex-employee :

Revaluation A/c	Dr.	10,000	
To Bank A/c			10,000

(III) Gaining Ratio 8 : 7

Q. 90. Harish, Paresh and Mahesh were three partners sharing profits and losses in the ratio of 5 : 4 : 1.

Paresh retired on 31st March, 2017. His capital as on 1st April, 2016, was ₹80,000. During the year 2016-17, he made drawings of ₹5,000. He was to be charged interest on drawings ₹100.

The partnership deed provides that on the retirement of a partner, he will be entitled to :

(*i*) His share of capital.

(*ii*) Interest on capital @ 10% per annum.

(*iii*) His share of profit in the year of retirement.

(*iv*) His share of goodwill of the firm.

(*v*) His share in the profit/loss on revaluation of assets and liabilities.

Additional information :

(*a*) Paresh's share in the profits of the firm for the year 2016-17 was ₹20,000.

(*b*) Goodwill of the firm was valued at ₹24,000.

(*c*) The firm suffered a loss of ₹12,000 on the revaluation of assets and liabilities.

(*d*) It was decided to transfer the amount due to Paresh to his loan account bearing interest @ 6% per annum. The loan was to be repaid in two equal annual instalments, the first instalment to be paid on 31st March, 2018.

You are required to prepare :

(*i*) Paresh's Capital Account.

(*ii*) Paresh's Loan Account till it is finally closed. *(I.S.C. 2018)*

[**Ans.** Net Amount due to Paresh ₹1,07,700;
Amount paid on 31st March 2018 : ₹53,850 + Interest ₹6,462
Amount paid on 31st March 2019 : ₹53,850 + Interest ₹3,231]

Q. 91. Mohit, Ali and John were partners in a firm, sharing profits and losses in the ratio of 3 : 1 : 1. Their Balance Sheet as at 31st March, 2018, was as follows :

BALANCE SHEET OF MOHIT, ALI AND JOHN
as at 31st March, 2018

Liabilities		₹	*Assets*		₹
Trade Creditors		15,000	Cash at Bank		40,000
General Reserve		6,000	Sundry Debtors	30,000	
Investment Fluctuation Fund		9,000	*Less* : Provision for		
Capital A/cs :			Doubtful Debts	(5,000)	25,000
Mohit	70,000		Investments		
Ali	50,000		(Market Value ₹40,000)		35,000

John	50,000	1,70,000	Plant & Machinery	88,000
			Goodwill	12,000
		2,00,000		2,00,000

Mohit retired on 1st April, 2018, subject to the following adjustments :

(*a*) Goodwill of the firm to be valued at ₹20,000.

(*b*) Mohit to take over the investments at the market value.

(*c*) 25% of the General Reserve to be transferred to Provision for Doubtful Debts and the balance to be distributed amongst all the partners.

(*d*) Creditors to be paid ₹3,000 less.

(*e*) Investment Fluctuation Fund not to be distributed. For this, it was decided that the remaining partners would compensate the retiring partner through their capital accounts.

(*f*) Mohit to be paid ₹20,000 immediately on retirement and the balance to be transferred to his loan account.

You are required to :

(*i*) Pass journal entries on the date of Mohit's retirement.

(*ii*) Prepare the Balance Sheet of the reconstituted firm. *(I.S.C. 2019)*

SOLUTION : **In the Books of Mohit, Ali & John**

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2018				₹	₹
April 1	Mohit's Capital A/c	Dr.		7,200	
	Ali's Capital A/c	Dr.		2,400	
	John's Capital A/c	Dr.		2,400	
	To Goodwill A/c				12,000
	(Goodwill existing in the books written off)				
	Ali's Capital A/c	Dr.		6,000	
	John's Capital A/c	Dr.		6,000	
	To Mohit's Capital A/c				12,000
	(Adjustment for goodwill in the gaining ratio of 1 : 1)				
	General Reserve A/c	Dr.		6,000	
	To Prov. for Doubtful Debts A/c				1,500
	To Mohit's Capital A/c				2,700
	To Ali's Capital A/c				900
	To John's Capital A/c				900
	(Adjustment for general reserve)				
	Investments A/c	Dr.		5,000	
	Trade Creditors A/c	Dr.		3,000	
	To Revaluation A/c				8,000
	(Gain on revaluation of assets and liabilities)				

Particulars		L.F.	Dr. ₹	Cr. ₹
Revaluation A/c	Dr.		8,000	
To Mohit's Capital A/c				4,800
To Ali's Capital A/c				1,600
To John's Capital A/c				1,600
(Gain on revaluation transferred to capital accounts)				
Ali's Capital A/c	Dr.		2,700	
John's Capital A/c	Dr.		2,700	
To Mohit's Capital A/c				5,400
(Adjustment for Mohit's share of Investment Fluctuation Fund)				
Mohit's Capital A/c	Dr.		40,000	
To Investments A/c				40,000
(Investments taken over by Mohit)				
Mohit's Capital A/c	Dr.		47,700	
To Bank A/c				20,000
To Mohit's Loan A/c				27,700
(Mohit's Capital A/c closed)				

BALANCE SHEET OF ALI & JOHN

as at 1st April, 2018

Liabilities		₹	*Assets*		₹
Trade Creditors		12,000	Cash at Bank		20,000
Investment Fluctuation Fund		9,000	Sundry Debtors	30,000	
Mohit's Loan A/c		27,700	*Less* : Provision for		
Capital A/cs :			Doubtful Debts	6,500	23,500
Ali	41,400		Plant & Machinery		88,000
John	41,400	82,800			
		1,31,500			1,31,500

Working Notes :

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*Mohit*	*Ali*	*John*	*Particulars*	*Mohit*	*Ali*	*John*
	₹	₹	₹		₹	₹	₹
To Goodwill	7,200	2,400	2,400	By Bal. b/d	70,000	50,000	50,000
To Mohit's Capital		6,000	6,000	By General Reserve	2,700	900	900
To Mohit's Capital		2,700	2,700	By Revaluation	4,800	1,600	1,600
To Investments	40,000			By Ali's Capital	6,000		
To Bank	20,000			By John's Capital	6,000		
To Mohit's Loan A/c	27,700			By Ali's Capital	2,700		
To Bal. c/d		41,400	41,400	By John's Capital	2,700		
	94,900	52,500	52,500		94,900	52,500	52,500

Death of a Partner

Q. 92. *P, R* and *S* are in partnership sharing profits 4/8, 3/8 and 1/8 respectively. It is provided under the partnership deed that on the death of any partner his share of goodwill is to be valued at one-half of the net profits credited to his account during the last 4 completed years (books of accounts are closed on 31st March).

R died on Ist April, 2022. The firm's profits for the last 4 years ending 31st March each year were as follows: 2019 Profits ₹1,20,000; 2020 Profits ₹60,000; 2021 Losses ₹20,000 and 2022 Profits ₹80,000.

(*i*) Determine the amount that should be credited to *R* in respect of his share of goodwill.

(*ii*) Pass a journal entry without raising goodwill account for its adjustment assuming that profit sharing ratio between *P* and *S* in future will be 3 : 2. Show your working clearly.

[**Ans.** *P*'s Capital A/c	Dr.	12,000	
S's Capital A/c	Dr.	33,000	
To *R*'s Capital A/c			45,000]

Q. 93. In the partnership agreement between *X, Y* and *Z* who were sharing profits in the ratio of 5 : 3 : 2, the goodwill was to be valued on the death of any partner on the basis of such partner's share of 2 years' profits calculated on the average of 5 years' profits immediately preceding the year of death less 10%. The firm's profits were 2016 ₹10,000; 2017 ₹30,000; 2018 ₹43,000 and in 2019 and 2020 losses of ₹6,000 and ₹4,000 respectively. The deceased partner's share of profits for the period of his life-time in the year of death was to be based on the average of the profits of the previous 3 years plus 10%.

X died on 31st August, 2020. His Capital A/c showed a credit of ₹50,000 on 1st April, 2020 and he had drawn ₹4,000 since that date.

Calculate the amount due to his legal representatives.

[**Ans.** Amount payable to *X*'s legal representatives ₹61,661]

Hint : *X*'s share of Goodwill ₹13,140; Share of Profit ₹2,521

Q. 94. *A, B* and *C* were partners. Their partnership deed provided that they were to share profits thus; *A* 26 per cent; *B* 34 per cent; *C* 40 per cent; and that if a partner died, his capital should remain in the business for a stated period at a fixed rate of interest, but that the deceased partner's share should be credited with an amount for Goodwill, based upon one and a half year's average profits, for the five years prior to his death, but be subject to deduction of 5 per cent from the book debts. *C* died, and the profits of the firm for five years were agreed at ₹20,000; ₹30,000; ₹15,000 (loss); ₹5,000 (loss); and ₹45,000 respectively. Book Debts stood at ₹90,000.

Prepare a statement showing the amount of Goodwill to be credited to *C*'s Account and give the Journal entry in the firm's book necessary to carry out the transactions.

[**Ans.** *C*'s Capital Account will be credited with ₹7,200]

Hint : Total Goodwill ₹22,500

Net Goodwill = 22,500 – 4,500 (5% of Book Debts) = ₹18,000

C's Share $= 18{,}000 \times \frac{40}{100} = ₹7{,}200$

Q. 95. *M*, *N* and *O* were partners in a firm sharing profits and losses equally. Their Balance Sheet as at 31st March, 2022 was as follows :

Liabilities		₹	*Assets*	₹
Capitals :			Plant and Machinery	60,000
M	70,000		Stock	30,000
N	70,000		Sundry Debtors	95,000
O	70,000	2,10,000	Cash at Bank	40,000
General Reserve		30,000	Cash in Hand	35,000
Creditors		20,000		
		2,60,000		2,60,000

N died on 12th June, 2022. According to the Partnership Deed, executors of the deceased partner are entitled to :

(*i*) Balance of partner's capital account.

(*ii*) Interest on Capital @5% p.a.

(*iii*) Share of goodwill calculated on the basis of twice the average of past three year's profits and

(*iv*) Share of profits from the closure of the last accounting year till the date of death on the basis of twice the average of three completed year's profits before death.

Profits for the years ended on 31st March, 2020, 2021 and 2022 were ₹80,000, ₹90,000 and ₹1,00,000 respectively. Show the working for deceased partner's share of goodwill and profits till the date of his death. Pass the necessary journal entries and prepare *N*'s Capital Account to be rendered to his executors.

[Ans. Amount due to *N*'s Executors ₹1,52,700.]

Hint : *N*'s share of Profit ₹12,000.

Q. 96. Hiren, Suren and Chaman were partners sharing profits and losses in the ratio of 2 : 1 : 1. They closed their books on 31st March each year. Hiren died on 31st August, 2013, when their Balance Sheet was as follows :

Liabilities		₹	*Assets*	₹
Creditors		4,550	Bank	22,000
General Reserve		6,400	Sundry Debtors	6,600
Profit for 5 months — from 1-4-13 to 31-8-13 (before interest and salaries)		4,050	Advertisement Suspense A/c	6,400
Capital Accounts :				
Hiren	6,000			
Suren	10,000			
Chaman	4,000	20,000		
		35,000		35,000

According to the partnership deed :

(*i*) Interest on capital was allowed to all partners @ 6% p.a.

(*ii*) Hiren and Chaman were entitled to salaries at ₹100 and ₹50 per month respectively.

(*iii*) In the event of death of a partner goodwill was to be valued at 3 year's purchase of the average net profits of 2 completed years preceding death. The net profits for the years 2011-12 and 2012-13 were ₹4,000 and ₹6,000 respectively.

Hiren's share was paid to his executors.

You are required to prepare :

(*i*) Hiren's Capital Account.

(*ii*) Hiren's Executor's Account. *(I.S.C. Sample Question Paper 2015)*

SOLUTION :

Dr. HIREN'S CAPITAL ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2013			2013		
Aug. 31	Advertisement Suspense A/c	3,200	Aug. 31	By Balance b/d	6,000
Aug. 31	To Hiren's Executor's A/c (balance transferred)	15,550	Aug. 31	By General Reserve	3,200
			Aug. 31	By Interest on Capital (6% on ₹6,000 for 5 months)	150
			Aug. 31	By Salary (₹100 × 5)	500
			Aug. 31	By P & L Appropriation A/c (Note 1)	1,400
			Aug. 31	By Suren's Capital A/c (Goodwill)	3,750
			Aug. 31	By Chaman's Capital A/c (Goodwill)	3,750
		18,750			18,750

Dr. HIREN'S EXECUTOR'S ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2013			2013		
Aug. 31	To Bank A/c	15,550	Aug. 31	By Hiren's Capital A/c	15,550

Working Notes :

			₹
(1)	Profit for 5 months		4,050
Less :	Interest on Capital 6% on (₹6,000 + ₹10,000 + ₹4,000) for 5 months : $20,000 \times \frac{6}{100} \times \frac{5}{12}$	500	
	Salary for 5 months : 5 × (100 + 50)	750	1,250
			2,800

Hiren's share of profit $= 2,800 \times \frac{2}{4} =$ ₹1,400

(2) Valuation of Goodwill :

Total profits for the two preceding years (₹4,000 + ₹6,000)		=	10,000
Average Profit = 10,000 ÷ 2		=	5,000
Goodwill at 3 year's purchase	= 5,000 × 3	=	15,000
Hiren's share of goodwill	$= 15,000 \times \frac{2}{4}$	=	7,500

It will be debited to Suren and Chaman in their gaining ratio *i.e.*, 1 : 1.

Q. 97. Ram, Krishna and Mohan are partners in a firm, sharing profits and losses in the ratio of 3 : 5 : 2. On 31st March, 2014, their Balance Sheet was as under :

BALANCE SHEET

as at 31st March, 2014

Liabilities		₹	*Assets*	₹
Creditors		39,200	Land and Building	48,000
General Reserve		16,000	Plant	72,000
Capital A/cs :			Inventory	34,000
Ram	76,800		Trade Marks	26,400
Krishna	69,600		Bills Receivables	39,200
Mohan	54,000	2,00,400	Cash in Hand	24,000
			Advertisement Suspense	12,000
		2,55,600		2,55,600

Krishna died on 30th September, 2014. An agreement was reached amongst Ram, Mohan and Krishna's legal representative that :

(*a*) Goodwill to be valued at 2 year's purchase of the average profits of the previous three years, which were :

Year :	2011-12	2012-13	2013-14
Profit :	₹31,200	₹28,800	36,000

(*b*) Trade marks to be revalued at ₹19,200; plant at 80% of its book value and land building at ₹57,600.

(*c*) Krishna's share of profit to the date of his death to be calculated on the basis of previous year's profit.

(*d*) Interest on capital to be provided @10% per annum.

(*e*) ₹60,080 to be paid in cash to Krishna's legal representative and balance to be transferred to the legal representative's loan account.

You are required to prepare :

(*i*) Revaluation Account.

(*ii*) Krishna's Capital Account, and

(*iii*) Krishna's Legal Representative's Account. *(I.S.C. 2015)*

[**Ans.** Amount transferred to Krishna's Legal Representative's Loan A/c ₹50,000.]

Q. 98. *X*, *Y* and *Z* were partners in a firm sharing profits and losses in the ratio of 5 : 3 : 2. On 31.3.2019 their Balance Sheet was as follows :

Liabilities		Amount	Assets	Amount
		₹		₹
Capital Accounts :			Building	50,000
X	75,000		Patents	15,000
Y	62,500		Machinery	75,000
Z	37,500	1,75,000	Stock	37,500
Sundry Creditors		42,500	Debtors	20,000
			Cash at Bank	20,000
		2,17,500		2,17,500

Z died on 31.7.2019. It was agreed that :

(*a*) Goodwill be valued at 2½ year's purchase of the average profits of the last four years, which were as follows :

Years	*Profits*
	₹
2015 – 16	32,500
2016 – 17	30,000
2017 – 18	40,000
2018 – 19	37,500

(*b*) Machinery be valued at ₹70,000; Patents at ₹20,000 and Building at ₹62,500.

(*c*) For the purpose of calculating *Z*'s share of profits in the year of his death the profits in 2019–20 should be taken to have been accrued on the same scale as in 2018–19.

(*d*) A sum of ₹17,500 was paid immediately to the executors of *Z* and the balance was paid in four half yearly instalments together with interest at 12% p.a. starting from 31.1.2020.

Give necessary journal entries to record the above transactions and *Z*'s executor's account till the payment of instalments due on 31.1.2020.

Note : The firm closes its accounts on 31st March every year.

SOLUTION : JOURNAL ENTRIES

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2019					
July 31	*X*'s Capital A/c	Dr.		10,938	
	Y's Capital A/c	Dr.		6,562	
	To *Z*'s Capital A/c(1)				17,500
	(*Z*'s share of goodwill adjusted into the Capital A/cs of existing partners in their gaining ratio of 5 : 3)				
July 31	Profit & Loss Suspense A/c	Dr.		2,500	
	To *Z*'s Capital A/c				2,500
	(Transfer of $\frac{2}{10}$th share of profit upto 31st July, 2010 *i.e.* ₹37,500 × $\frac{4}{12} \times \frac{2}{10}$)				

July 31	Revaluation A/c To Machinery A/c (Decrease in the value of machinery)	Dr.	5,000	5,000
July 31	Patents A/c Building A/c To Revaluation A/c (Increase in the value of Patents and Building)	Dr. Dr.	5,000 12,500	17,500
July 31	Revaluation A/c To *X*'s Capital A/c To *Y*'s Capital A/c To *Z*'s Capital A/c (Profit on revaluation transferred to partners capital accounts)	Dr.	12,500	6,250 3,750 2,500
July 31	*Z*'s Capital A/c To *Z*'s Executor's A/c (Amount due to *Z* transferred to his executor's account)	Dr.	60,000	60,000
July 31	*Z*'s Executor's A/c To Bank A/c (Part payment to *Z*'s executor's)	Dr.	17,500	17,500

Dr. *Z*'s CAPITAL A/C Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2019			2019		
July 31	To *Z*'s Executor's A/c	60,000	April 1	By Balance b/d	37,500
			July 31	By *X*'s Capital A/c (Goodwill)	10,938
			July 31	By *Y*'s Capital A/c (Goodwill)	6,562
			July 31	By Profit & Loss Suspense A/c	2,500
			July 31	By Revaluation A/c	2,500
		60,000			60,000

Dr. *Z*'s EXECUTOR'S ACCOUNT Cr.

Date	*Particulars*	₹	*Date*	*Particulars*	₹
2019			2019		
July 31	To Bank A/c	17,500	July 31	By *Z*'s Capital A/c	60,000
2020			2020		
Jan. 31	To Bank A/c (10,625[(2)] + 2,550)	13,175	Jan. 31	By Interest A/c (₹42,500 × 12/100 × 6/12)	2,550
Jan. 31	To Balance c/d	31,875			
		62,550			62,550

2020 Mar. 31	To Balance c/d	32,513	2020 Feb. 1	By Balance b/d		31,875
			Mar. 31	By Interest A/c* $(31,875 \times \frac{12}{100} \times \frac{2}{12})$		638
		32,513				32,513

Notes : (1) Calculation of Goodwill :

				₹
	Total Profit	=	32,500 + 30,000 + 40,000 + 37,500 =	1,40,000
	Average Profit	=	₹1,40,000 ÷ 4 =	35,000
Hence,	Goodwill	=	₹35,000 × $2\frac{1}{2}$ =	87,500
	Z's Share	=	₹87,500 × $\frac{2}{10}$ =	17,500

(2) ₹42,500 ÷ 4 = ₹10,625

* ₹638 is the amount of interest accrued but not due.

Q. 99. Karan, Ali and Deb are partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. On 31st March, 2016, their Balance Sheet was as under :

BALANCE SHEET OF KARAN, ALI AND DEB

as at 31st March, 2016

Liabilities		₹	*Assets*		₹
Capital A/cs			Building		1,00,000
Karan	1,00,000		Furniture		40,000
Ali	75,000		Investments		50,000
Deb	50,000	2,25,000	Debtors	30,000	
Investment Fluctuation Reserve		30,000	*Less :* Provision for		
Bills Payable		10,000	Doubtful		
Creditors		15,000	Debts	1,000	29,000
			Cash at Bank		43,000
			Goodwill		18,000
		2,80,000			2,80,000

Karan died on 1st July, 2016. An agreement was reached among Ali, Deb and Karan's legal repesentatives that :

(a) Building be revalued at ₹93,500.

(b) Furniture be appreciated by ₹10,000.

(c) To write off the Provision for Doubtful Debts since all debtors are good.

(d) Investments be valued at ₹38,000.

(e) Goodwill of the firm be valued at ₹1,20,000.

(f) Karan's share of profit to the date of his death, to be calculated on the basis of previous year's profit which was ₹25,000.

(g) Interest on capital to be allowed on Karan's capital @ 6% per annum.

(h) Amount payable to Karan's legal representative to be transferred to his legal representative's loan account.

You are required to :

(i) Pass journal entries on the date of Karan's death.

(ii) Prepare the Interim Balance Sheet of the reconstituted firm.

(I.S.C. 2017)

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2016					
July 1	Karan's Capital A/c	Dr.		9,000	
	Ali's Capital A/c	Dr.		6,000	
	Deb's Capital A/c	Dr.		3,000	
	To Goodwill A/c				18,000
	(Goodwill written off)				
	Revaluation A/c	Dr.		6,500	
	To Building A/c				6,500
	(Decrease in the value of Building)				
	Furniture A/c	Dr.		10,000	
	Prov. for Doubtful Debts A/c	Dr.		1,000	
	To Revaluation A/c				11,000
	(Increase in the value of assets)				
	Revaluation A/c	Dr.		4,500	
	To Karan's Capital A/c				2,250
	To Ali's Capital A/c				1,500
	To Deb's Capital A/c				750
	(Gain on revaluation transferred to Partner's Capital Accounts)				
	Investment Fluctuation Reserve A/c	Dr.		30,000	
	To Investmens A/c				12,000
	To Karan's Capital A/c				9,000
	To Ali's Capital A/c				6,000
	To Deb's Capital A/c				3,000
	(Loss in the value of investments written off)				
	Ali's Capital A/c	Dr.		40,000	
	Deb's Capital A/c	Dr.		20,000	
	To Karan's Capital A/c				60,000
	(Karan's share of goodwill adjusted through the gaining partner's capital accounts)				
	P & L Suspense A/c(1)	Dr.		3,125	
	To Karan's Capital A/c				3,125
	(Karan's share of Profits credited to his Capital A/c)				

Interest on Capital A/c[2] Dr. To Karan's Capital A/c (Interest on capital allowed to Karan)			1,500	1,500
P & L Suspense A/c Dr. To Interest on Capital A/c (Transfer of interest on Capital to P & L Suspense A/c)			1,500	1,500
Karan's Capital A/c Dr. To Karan's Executor's Loan A/c (Transfer of amount due to Karan)			1,66,875	1,66,875

Dr. **PARTNER'S CAPITAL ACCOUNTS** Cr.

Particulars	*Karan* ₹	*Ali* ₹	*Deb* ₹	*Particulars*	*Karan* ₹	*Ali* ₹	*Deb* ₹
To Goodwill	9,000	6,000	3,000	By Balance b/d	1,00,000	75,000	50,000
To Karan's Capital A/c		40,000	20,000	By Investment Fluctuation Res.	9,000	6,000	3,000
To Karan's Executor's Loan A/c	1,66,875			By Revaluation A/c	2,250	1,500	750
To Balance c/d		36,500	30,750	By Ali's Capital A/c	40,000		
				By Deb's Capital A/c	20,000		
				By P & L Suspense A/c	3,125		
				By Interest on Capital	1,500		
	1,75,875	82,500	53,750		1,75,875	82,500	53,750

BALANCE SHEET OF ALI AND DEB
as at 1st July, 2016

Liabilities		₹	*Assets*		₹
Capital A/cs :			Building		93,500
Ali	36,500		Furniture		50,000
Deb	30,750	67,250	Investments		38,000
Bills Payable		10,000	Debtors		30,000
Creditors		15,000	Cash at Bank		43,000
Karan's Executor's Loan A/c		1,66,875	P & L Suspense :		
			Share of Profit	3,125	
			Interest on Capital	1,500	4,625
		2,59,125			2,59,125

Working Notes :

(1) Karan's share of profit $= 25{,}000 \times \frac{3}{12} \times \frac{3}{6} = ₹3{,}125$

(2) Interest on Capital $= 1{,}00{,}000 \times \frac{6}{100} \times \frac{3}{12} = ₹1{,}500$

Q. 100. Ravi, Sam and Tukai were in partnership sharing profits and losses in the ratio of 6 : 5 : 4. The annual rent due to Sam for using his personal property for the use of the business is ₹9,000 and this is treated as a business expense.

Accounts of the business are closed annually on 31st March.

The partnership deed provides that the representatives of a deceased partner are entitled to :

(*a*) The deceased partner's capital as appearing in the last Balance Sheet.

(*b*) Interest on capital @ 6% per annum to the date of his death.

(*c*) Interest on drawings @ 5% per annum.

(*d*) His share of profits calculated till the date of his death on the average of the last three years' profits.

(*e*) Share of goodwill calculated at two years' purchase of the average profits for the last three years prior to charging the rent but after charging interest on capital.

The profits of the firm for the years 2014-15, 2015-16 and 2016-17 after charging rent and interest on capital amounted to ₹62,000, ₹63,000 and ₹73,000 respectively.

Sam died on 30th June, 2017.

His drawings from 1st April 2017 to the date of his death amounted to ₹3,000.

His capital shown in the Balance Sheet of 31st March 2017, was ₹90,000.

You are required to prepare Sam's Capital Account to show the amount due to his estate from the firm. *(I.S.C. Specimen Question Paper, 2018)*

SOLUTION :

Dr. SAM'S CAPITAL ACCOUNT Cr.

Date	Particulars	₹	Date	Particulars	₹
2017			2017		
June 30	To Drawings	3,000	April 1	By Balance b/d	90,000
June 30	To Interest on Drawings(2)	19	June 30	By Interest on Capital(1)	1,350
June 30	To Sam's Executor's A/c (Balance transferred)	1,46,081	June 30	By Profit & Loss Suspense A/c(3)	5,500
			June 30	By Rent(4)	2,250
			June 30	By Ravi's Capital (Goodwill)	30,000
			June 30	By Tukai's Capital (Goodwill)	20,000
		1,49,100			1,49,100

Working Notes :

(1) Interest on Capital for 3 months = 90,000 × $\frac{6}{100}$ × $\frac{3}{12}$ = ₹1,350

(2) Since the date of drawings is not given, interest on drawings will be calculated for an average period of $\frac{1}{2}$ of 3 months = 1.5 months.

$$3{,}000 \times \frac{5}{100} \times \frac{1.5}{12} = ₹19$$

(3) Sam's share of profit upto the date of his death :

Average Profits = $\frac{62{,}000 + 63{,}000 + 73{,}000}{3}$ = ₹66,000

Share of Profit = 66,000 × $\frac{3}{12}$ × $\frac{5}{15}$ = ₹ 5,500

(4) Rent due for 3 months = 9,000 × $\frac{3}{12}$ = ₹2,250

(5) Calculation of Sam's share of Goodwill :

			₹
Average Profit after charging Rent		=	66,000
+ Rent			9,000
Average Profit prior to charging Rent		=	75,000
Goodwill at 2 year's purchase	= ₹75,000 × 2	=	1,50,000
Sam's share of goodwill	= ₹1,50,000 × $\frac{5}{15}$	=	50,000

It will be contributed by Ravi and Tukai in their gaining ratio of 6 : 4.

Thus Ravi's Contribution = 50,000 × $\frac{6}{10}$ = ₹30,000

Tukai's Contribution = 50,000 × $\frac{4}{10}$ = ₹20,000

MULTIPLE CHOICE QUESTIONS

Select the Best Alternate :

1. Retiring partner is compensated for parting with the firm's future profits in favour of remaining partners. The remaining partners contribute to such compensation amount in :
   (A) Gaining Ratio (B) Capital Ratio
   (C) Sacrificing Ratio (D) Profit Sharing Ratio

2. 'Gaining Ratio' means :
   (A) Old Ratio – New Ratio (B) New Ratio – Old Ratio
   (C) Old Ratio – Sacrificing Ratio (D) New Ratio – Sacrificing Ratio

3. What treatment is made of accumulated profits and losses on the retirement of a partner?
   (A) Credited to all partner's capital accounts in old ratio.
   (B) Debited to all partner's capital accounts in old ratio.
   (C) Credited to remaining partner's capital accounts in new ratio.
   (D) Credited to remaining partner's capital accounts in gaining ratio.

4. At the time of retirement of a partner, profit on revaluation will be credited to :
   (A) Capital Account of retiring partner
   (B) Capital Accounts of all partners in the old profit sharing ratio.
   (C) Capital Accounts of the remaining partners in their old profit sharing ratio
   (D) Capital Accounts of the remaining partners in their new profit sharing ratio

5. What journal entry will be recorded for writing off the goodwill already existing in Balance Sheet at the time of retirement of a partner?

(A)	Retiring Partner's Capital A/c To Goodwill A/c	Dr.
(B)	All Partner's Capital A/cs (including retiring) To Goodwill A/c	Dr. (in old ratio)
(C)	Remaining Partner's Capital A/cs To Goodwill A/c	Dr. (in gaining ratio)
(D)	Remaining Partner's Capital A/cs To Goodwill A/c	Dr. (in new ratio)

6. What journal entry will be recorded for deceased partner's share in profit from the closure of last balance sheet till the date of his death?

(A)	Profit and Loss A/c To Deceased Partner's Capital A/c	Dr.
(B)	Deceased Partner's Capital A/c To Profit and Loss A/c	Dr.
(C)	Deceased Partner's Capital A/c To Profit and Loss Suspense A/c	Dr.
(D)	Profit and Loss Suspense A/c To Deceased Partner's Capital A/c	Dr.

7. On retirement of a partner, goodwill will be credited to the Capital Account of:
   (A) Retiring Partner (B) Remaining Partners
   (C) All Partners (D) None of the Above

8. On the death of a partner, the amount due to him will be credited to :
   (A) All partner's Capital Accounts
   (B) Remaining partner's Capital Accounts
   (C) His Executor's Account
   (D) Governments' Revenue Account

9. How goodwill is recorded on the retirement of a partner?

(A)	Remaining Partner's Capital A/cs To Retiring Partner's Capital A/c	Dr. (In Gaining Ratio) (with his share of goodwill)
(B)	Remaining Partner's Capital A/cs To Retiring Partner's Capital A/c	Dr. (In New Ratio) (with his share of goodwill)

(C) Goodwill A/c Dr.
To All Partner's Capital A/cs (In Old Ratio)

(D) Goodwill A/c Dr.
To Retiring Partner's Capital A/c (with his share)

10. *A*, *B* and *C* are partners in 3 : 4 : 2. *B* wants to retire from the firm. The profit on revaluation on that date was ₹36,000. New ratio of *A* and *C* is 5 : 3. Profit on revaluation will be distributed as :
(A) *A* ₹16,000; *B* ₹12,000; *C* ₹8,000
(B) *A* ₹12,000; *B* ₹16,000; *C* ₹8,000
(C) *A* ₹22,500; *C* ₹13,500
(D) *A* ₹23,625; *C* ₹12,375

11. *A*, *B* and *C* are partners sharing profits in the ratio of 5 : 2 : 1. If the new ratio on the retirement of *A* is 3 : 2, what will be the gaining ratio?
(A) 11 : 14 (B) 3 : 2
(C) 2 : 3 (D) 14 : 11

12. *P*, *Q* and *R* are partners sharing profits in the ratio of 5 : 4 : 3. *Q* retires and *P* and *R* decide to share future profits equally. Gaining Ratio will be :
(A) 5 : 3 (B) 1 : 1
(C) 1 : 3 (D) 3 : 1

13. *A*, *B* and *C* are partners sharing profits in the ratio of 1/2 : 1/4 : 1/4. New ratio on the retirement of *B* will be :
(A) 2 : 4 (B) 1 : 2
(C) 2 : 1 (D) 1/4 : 1/2

14. *A*, *B* and *C* are partners sharing profits in the ratio of 1/4 : 3/10 : 9/20. The New ratio on the retirement of *C* will be :
(A) 6 : 5 (B) 5 : 6
(C) 4 : 3 (D) 4 : 10

15. *X*, *Y* and *Z* have been sharing profits in the ratio of 4 : 2 : 1 *Z* retires. *X* and *Y* take *Z*'s share equally. New profit sharing ratio will be :
(A) 5 : 2 (B) 5 : 3
(C) 9 : 5 (D) 4 : 2

16. *P*, *Q* and *R* have been sharing profits and losses in the ratio of 5 : 3 : 2. *Q* retires. His share is taken by *P* and *R* in the ratio of 2 : 1. New profit sharing ratio will be:
(A) 6 : 4 (B) 7 : 3
(C) 7 : 2 (D) 6 : 3

17. *A*, *B* and *C* share profits and losses of the firm equally. *B* retires from business and his share is purchased by *A* and *C* in the ratio of 2 : 3. New profit sharing ratio between *A* and *C* respectively would be :
(A) 01 : 01 (B) 02 : 02
(C) 07 : 08 (D) 03 : 05

18. P, Q and R have been sharing profits in the ratio of 8 : 5 : 3. P retires. Q takes 3/16th share from P and R takes 5/16th share from P. New profit sharing ratio will be :
(A) 1 : 1
(B) 10 : 6
(C) 9 : 7
(D) 5 : 3

19. A, B and C are equal partners. C retires. He surrenders 3/5th of his share in favour of A and 2/5th in favour of B. New ratio will be :
(A) 3 : 2
(B) 8 : 7
(C) 7 : 8
(D) 2 : 3

20. P, Q and R are partners sharing profits in the ratio of 4 : 3 : 2. Q retires and his share was taken up by P and R in the ratio 3 : 2. New profit sharing ratio will be :
(A) 16 : 29
(B) 29 : 16
(C) 3 : 2
(D) 2 : 3

21. Srishti, Nitya and Anand were partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. Srishti retired from the firm selling her share of profits to Nitya and Anand in the ratio of 2 : 1. The new profit sharing ratio between Nitya and Anand will be :
(A) 3 : 2
(B) 17 : 11
(C) 2 : 1
(D) 19 : 11
(C.B.S.E. 2020, Lucknow, Kolkata)

22. Amla, Bimla and Kavita were partners sharing profits and losses in the ratio of 4 : 3 : 1. Bimla retired and gives her share of profit to Amla for ₹3,600 and to Kavita for ₹3,000. The gaining ratio of Amla and Kavita will be :
(A) 4 : 5
(B) 2 : 1
(C) 6 : 5
(D) 4 : 1 *(C.B.S.E. 2020, Punjab)*

23. L, P and G are three partners sharing profits in the ratio 15 : 9 : 8. G retires. L and P decided to share profits in equal ratio. Gaining ratio will be :
(A) 15 : 9
(B) 9 : 15
(C) 7 : 1
(D) 1 : 7

24. On 1st April, 2019 A, B and C were partners sharing profits and losses in the ratio of 5 : 3 : 2 respectively. On this date B retires. The new profit sharing ratio of A and C will be 3 : 2. Gaining ratio will be :
(A) 1 : 2
(B) 2 : 1
(C) 1 : 1
(D) 5 : 2

25. B, P and L sharing profits in the ratio 4 : 3 : 2. B retires, P and L decided to share profits in future in the ratio of 5 : 3. Gaining ratio will be :
(A) 11 : 21
(B) 21 : 11
(C) 11 : 13
(D) 13 : 11

26. P, Q and R were partners sharing profits in the ratio 2 : 2 : 1. Q retires and the new profit sharing ratio of P and R will be 3 : 1. Gaining ratio will be :
(A) 1 : 7
(B) 2 : 1
(C) 1 : 2
(D) 7 : 1

27. *A*, *B* and *C* are equal partners in a firm. *B* retires and the remaining partners decide to share the profits of the new firm in the ratio of 5 : 4. Gaining ratio will be :
    (A) 1 : 1 (B) 1 : 2
    (C) 2 : 1 (D) 5 : 4
28. *A*, *B* and *C* are partners sharing profit or loss in the ratio of 3 : 2 : 1. *B* retires and after *B*'s retirement *A* and *C* agreed to share profit or loss in the ratio of 3 : 2 in future. Their gaining ratio will be :
    (A) 3 : 1 (B) 1 : 3
    (C) 3 : 7 (D) None of the above
29. *A*, *B* and *C* are partners sharing profit or loss in the ratio of 4 : 3 : 2. *C* retires and after *C*'s retirement *A* and *B* agreed to share profit or loss in the ratio of 4 : 3 in future. Their gaining ratio will be :
    (A) 3 : 2 (B) 4 : 3
    (C) 3 : 4 (D) 1 : 1
30. *A*, *B* and *C* are partners sharing profit or loss in the ratio of 2 : 3 : 4. *A* retires and after *A*'s retirement *B* and *C* agreed to share profit or loss in the ratio of 3 : 4 in future. Their gaining ratio will be :
    (A) 2 : 3 (B) 4 : 3
    (C) 3 : 4 (D) 1 : 1

HOTS

31. *A*, *B* and *C* were partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1. The capital balance are ₹50,000 for *A*, ₹70,000 for *B*, ₹35,000 for *C*. *B* decided to retire from the firm and balance in reserve on the date was ₹25,000. If goodwill of the firm was valued at ₹30,000 and profit on revaluation was ₹7,500 then, what amount will be payable to *B*?
    (A) ₹70,820 (B) ₹76,000
    (C) ₹75,000 (D) ₹95,000

HOTS

32. *P*, *Q* and *R* are sharing profits and losses equally. *R* retires and the goodwill is appearing in the books at ₹30,000. Goodwill of the firm is valued at ₹1,50,000. Calculate the net amount to be credited to *R*'s Capital A/c.
    (A) ₹60,000 (B) ₹50,000
    (C) ₹40,000 (D) ₹10,000
33. Ram, Krishna and Ganesh were sharing profits and losses in the ratio of 5 : 3 : 2. Ram retires and Krishna and Ganesh share the future profits and losses equally. Goodwill of the firm is valued at ₹1,00,000. Calculate the amount of goodwill to be debited to Krishna's and Ganesha's Capital A/c.
    (A) ₹60,000 & ₹40,000 (B) ₹20,000 & ₹30,000
    (C) ₹40,000 & ₹60,000 (D) ₹30,000 & ₹20,000
34. *A*, *B* and *C* are partners with profit sharing ratio 4 : 3 : 2. *B* retires and goodwill was valued ₹1,08,000. If *A* & *C* share profits in 5 : 3, find out the goodwill shared by *A* and *C* in favour of *B*.

(A) ₹22,500 and ₹13,500 (B) ₹16,500 and ₹19,500
(C) ₹67,500 and ₹40,500 (D) ₹19,500 and ₹16,500

35. *A*, *B* and *C* are sharing profits in the ratio of 3 : 2 : 1. *B* retires and on the day of *B*'s retirement Goodwill is valued at ₹60,000. *A* and *C* decided to share future profits in the ratio of 3 : 2. Journal entry will be :

(A)

A's Capital A/c	Dr.	18,000	
C's Capital A/c	Dr.	42,000	
To *B*'s Capital A/c			60,000

(B)

A's Capital A/c	Dr.	6,000	
C's Capital A/c	Dr.	14,000	
To *B*'s Capital A/c			20,000

(C)

A's Capital A/c	Dr.	36,000	
C's Capital A/c	Dr.	24,000	
To *B*'s Capital A/c			60,000

(D)

A's Capital A/c	Dr.	12,000	
C's Capital A/c	Dr.	8,000	
To *B*'s Capital A/c			20,000

36. *P*, *Q* and *R* share profits in the ratio of 5 : 4 : 3. *R* retires and the new ratio is 5 : 3. If *R* is given ₹6,000 as goodwill, journal entry will be :

(A)

P's Capital A/c	Dr.	1,000	
Q's Capital A/c	Dr.	5,000	
To *R*'s Capital A/c			6,000

(B)

P's Capital A/c	Dr.	5,000	
Q's Capital A/c	Dr.	1,000	
To *R*'s Capital A/c			6,000

(C)

P's Capital A/c	Dr.	3,750	
Q's Capital A/c	Dr.	2,250	
To *R*'s Capital A/c			6,000

(D)

P's Capital A/c	Dr.	3,333	
Q's Capital A/c	Dr.	2,667	
To *R*'s Capital A/c			6,000

37. *X*, *Y* and *Z* were partners in a firm sharing profits in the ratio of 3 : 2 : 1. *X* retired and the new profit sharing ratio between *Y* and *Z* will be 5 : 4. On *X*'s retirement the goodwill of the firm was valued at ₹54,000. Journal entry will be :

(A)

Y's Capital A/c	Dr.	24,000	
Z's Capital A/c	Dr.	30,000	
To *X*'s Capital A/c			54,000

(B)

Y's Capital A/c	Dr.	15,000	
Z's Capital A/c	Dr.	12,000	
To *X*'s Capital A/c			27,000

(C) *Y*'s Capital A/c Dr. 12,000
Z's Capital A/c Dr. 15,000
To *X*'s Capital A/c 27,000

(D) *X*'s Capital A/c Dr. 27,000
To *Y*'s Capital A/c 12,000
To *Z*'s Capital A/c 15,000

38. *A*, *B* and *C* are partners sharing profits in the ratio of 3 : 4 : 5. *B* retires and the goodwill of the firm is valued at ₹42,000. *A* and *C* decide to share profits in the ratio of 3 : 4. Journal entry will be :

(A) *A*'s Capital A/c Dr. 6,000
C's Capital A/c Dr. 8,000
To *B*'s Capital A/c 14,000

(B) *A*'s Capital A/c Dr. 7,500
C's Capital A/c Dr. 6,500
To *B*'s Capital A/c 14,000

(C) *A*'s Capital A/c Dr. 22,500
C's Capital A/c Dr. 19,500
To *B*'s Capital A/c 42,000

(D) *B*'s Capital A/c Dr. 14,000
To *A*'s Capital A/c 7,500
To *C*'s Capital A/c 6,500

39. *P*, *Q* and *R* were partners sharing profits in the ratio 5 : 3 : 2 respectively. *P* retires from the firm and *Q* and *R* decide to share future profits equally. Goodwill is valued at ₹50,000.
Adjustment entry for goodwill will be :

(A) *Q*'s Capital A/c Dr. 15,000
R's Capital A/c Dr. 10,000
To *P*'s Capital A/c 25,000

(B) *Q*'s Capital A/c Dr. 20,000
R's Capital A/c Dr. 30,000
To *P*'s Capital A/c 50,000

(C) *Q*'s Capital A/c Dr. 12,500
R's Capital A/c Dr. 12,500
To *P*'s Capital A/c 25,000

(D) *Q*'s Capital A/c Dr. 10,000
R's Capital A/c Dr. 15,000
To *P*'s Capital A/c 25,000

40. *X*, *Y* and *Z* are partners sharing profits in the ratio of 2 : 3 : 5. Goodwill is already appearing in their books at a value of ₹60,000. *X* retires and *Y* and *Z* decided to share future profits equally. Journal entry will be :

(A) Y's Capital A/c	Dr.	12,000	
To X's Capital A/c			12,000
(B) Y's Capital A/c	Dr.	60,000	
To X's Capital A/c			60,000
(C) X's Capital A/c	Dr.	2,400	
Y's Capital A/c	Dr.	3,600	
Z's Capital A/c	Dr.	6,000	
To Goodwill A/c			12,000
(D) X's Capital A/c	Dr.	12,000	
Y's Capital A/c	Dr.	18,000	
Z's Capital A/c	Dr.	30,000	
To Goodwill A/c			60,000

HOTS

41. *A*, *B* and *C* are partners in a firm sharing profit/loss in the ratio of 2 : 2 : 1. On March 31, 2019, *C* died. Accounts are closed on Dec., 31 every year. The sales for the year 2018 was ₹6,00,000 and the profits were ₹60,000. The sales for the period from Jan. 1, 2019 to March 31, 2019 were ₹2,00,000. The share of deceased partner in the current year's profits on the basis of sales is :
   (A) ₹20,000 (B) ₹8,000
   (C) ₹ 3,000 (D) ₹4,000

HOTS

42. *A*, *B* and *C* were partners sharing profits and losses in the ratio of 2 : 2 : 1. Books are closed on 31st March every year. *C* dies on 5th November, 2018. Under the partnership deed, the executors of the deceased partner are entitled to his share of profit to the date of death, calculated on the basis of last year's profit. Profit for the year ended 31st March, 2018 was ₹2,40,000. *C*'s share of profit will be :
   (A) ₹28,000 (B) ₹32,000
   (C) ₹28,800 (D) ₹48,000

HOTS

43. *P*, *Q* and *R* were partners sharing profits in the ratio of their Capital contribution which were ₹6,00,000; ₹4,00,000 and ₹5,00,000 respectively. Their books are closed on 31st March every year. *P* dies on 24th August, 2018. Under the partnership deed, deceased partner is entitled to his share of profit/loss to the date of death based on the average profits of preceding three years. Profits were 2015 ₹50,000; 2016 ₹1,80,000 (Loss); 2017 ₹30,000 and 2018 ₹60,000. *P*'s share of profit/loss will be :
   (A) (₹ 3,200) (B) (₹6,400)
   (C) (₹12,000) (D) (₹4,800)

44. At what rate is interest payable on the amount remaining unpaid to the executor of deceased partner, in absence of any agreement among partners, when he opts for interest and not share of profit :

(A) 12% p.a. (B) 8% p.a.
(C) 6% p.a. (D) 7.5% p.a.

(C.B.S.E. Sample Paper, 2020)

45. *A*, *B* and *C* are partners in a firm sharing profit/loss in the ratio of 3 : 2 : 1. On March 31, 2019, *C* died. Accounts are closed on Dec., 31 every year. The sales for the year 2018 was 10,00,000 and the profits were 2,00,000. The sales for the period from Jan. 1, 2019 to March 31, 2019 were ₹3,00,000. The share of deceased partner in the current year's profits on the basis of sales is :

(A) ₹ 2,500 (B) ₹10,000
(C) ₹15,000 (D) ₹60,000

(C.B.S.E. 2019, Comptt.)

46. *A*, *B* and *C* were partners in a firm sharing profits and losses in the ratio of 5 : 3 : 2. *C* retired and his capital balance after adjustments regarding reserves, accumulated profits/losses and his share of gain on revaluation was ₹2,50,000. *C* was paid ₹3,22,000 including his share of goodwill. The amount credited to *C*'s Capital Account, on his retirement, for goodwill will be :

(A) ₹72,000 (B) ₹ 7,200
(C) ₹14,400 (D) ₹3,22,000

(C.B.S.E. 2020, Chennai, Mumbai)

47. In the case of retirement, if full or part of the amount payable to the retiring partner still remains to be paid, and there is no agreement among the partners then retiring partner will get :

(*i*) Interest @ 6% p.a. on the Balance amount.

(*ii*) Share of profit earned proportionate to his amount outstanding to total capital of the firm.

(*iii*) Interest @ 9% p.a. on the balance amount.

Which out of the following is correct?

(A) (*i*) (B) (*ii*)
(C) (*iii*) (D) Have a choice to get either (*i*) or (*ii*)

(C.B.S.E. 2020; Punjab)

48. Rajat, Mishi and Tanvi were partners in a firm sharing profits and losses in the ratio of 5 : 3 : 2. Tanvi died on 31st October, 2019. According to the partnership agreement, her share of profits from the closure of last accounting year till the date of her death was to be calculated on the basis of aggregate profits of two completed years before death. Profits of the firm for the years ending 31st March, 2018 and 31st March, 2019 were ₹57,000 and ₹63,000 respectively. The firm closes its books on 31st March every year. Tanvi's share of profits till the date of her death will be :

(A) ₹24,000 (B) ₹ 7,000
(C) ₹14,000 (D) ₹12,000

(C.B.S.E. 2020, Rajasthan)

[See answers at the end of the book.]

5

Dissolution of Partnership Firm

LEARNING OBJECTIVES

After studying this Chapter you should be able to understand :

- **Distinction between Dissolution of Partnership and Dissolution of Firm**
- **Modes of Dissolution of Firm**
- **Settlement of Accounts on Dissolution of Firm**
- **Accounting Treatment on Dissolution of Firm**
- **Distinction between Revaluation Account and Realisation Account**

Indian Partnership Act makes a distinction between dissolution of partnership and dissolution of partnership firm. **Dissolution of partnership means** termination of the old partnership agreement and a reconstruction of the firm due to admission, retirement and death of a partner. Dissolution of partnership may or may not result into closing down of the business as the remaining partners may agree to carry on the business under a new agreement.

Dissolution of partnership 'firm' means that the firm closes down its business and comes to an end. On the dissolution of the firm, the assets of the firm are sold and liabilities are paid off and out of the remaining amount, the accounts of partners are settled.

Thus, in case of dissolution of partnership, the firm may continue, *i.e.*, it does not mean the dissolution of firm. But in case of dissolution of the firm, the partnership is automatically dissolved.

Dissolution of Partnership

The partnership is deemed to have been dissolved in any of the following cases :

(*i*) In case of change in the profit-sharing ratio of the existing partners

(*ii*) In case of admission of a new partner

(*iii*) In case of retirement of a partner

(*iv*) In case of expulsion of a partner

(*v*) In case of death of a partner

(*vi*) In case of insolvency of a partner

(*vii*) In case of expiry of the period of partnership

Dissolution of Partnership Firm

Modes of Dissolution of Partnership Firm

A partnership firm can be dissolved in any of the following ways :

(A) Without the Intervention of the Court

1. **By Mutual Agreement (Sec. 40) :** A partnership firm may be dissolved when all the partners agree for its dissolution. Since a partnership firm is set up by an agreement, it can be dissolved by an agreement.
2. **Compulsory Dissolution (Sec. 41) :** A firm is compulsorily dissolved in the following cases :
   (*i*) When all or all but one partner of the firm becomes insolvent.
   (*ii*) When business of the firm becomes unlawful.
3. **On Happening of an Event (Sec. 42) :** A firm may be dissolved on the happening of any one of the following incidents :
   (*i*) On the insolvency of a partner.
   (*ii*) On the fulfilment of the object for which the firm was formed.
   (*iii*) On the expiry of the period for which the firm was formed.
4. **By Notice (Sec. 43) :** When the duration of the partnership firm is not fixed and it is at will, any partner by giving notice to other partners can dissolve the firm.

(B) By order of the Court (Sec. 44) : The Court may, on an application by a partner, order the dissolution of the partnership firm under the following circumstances :

(*i*) When a partner has become of unsound mind.
(*ii*) When a partner, other than the partner filing a suit, has become permanently incapable of performing his duties as a partner.
(*iii*) When a partner, other than the partner filing a suit, is guilty of misconduct that may harm the partnership.
(*iv*) When a partner, other than the partner filing a suit, wilfully or persistently commits breach of partnership agreement.
(*v*) When a partner, other than the partner filing a suit, has transferred the whole of his interests in the firm to a third party.
(*vi*) When the court is satisfied that the firm cannot be carried on except at a loss.
(*vii*) When the Court is satisfied that the dissolution is just and equitable due to some other reasons.

Distinction between Dissolution of Partnership and Dissolution of Firm

S. No.	*Basis of Distinction*	*Dissolution of Partnership*	*Dissolution of Firm*
1.	**Meaning**	It refers to a change in the existing agreement between the partners. The firm continues its business.	It refers to closure of the firm.

2.	**Continuation of the business**	The firm continues its business.	Business of the firm comes to an end.
3.	**Economic Relationship**	Economic relationship between the partners continues though in a changed form.	Economic relationship between the partners comes to an end.
4.	**Closure of Books of Accounts**	Books of accounts need not be closed.	Books of accounts have to be closed.
5.	**Settlement of Assets and Liabilities**	Assets are revalued and liabilities reassessed and gain or loss on revaluation is distributed among the partners in their old profit sharing ratio.	Assets are sold and liabilities are paid off and balance, if any, is distributed among all the partners.
6.	**Effect**	Dissolution of partnership does not necessarily means the dissolution of firm.	Dissolution of firm necessarily means the dissolution of partnership also.
7.	**Court's intervention**	There is no intervention by the court since the partnership is dissolved by mutual consent.	A firm can be dissolved either without the intervention of the court or by order of the court.

Settlement of Accounts on Dissolution

Sections 48 of the partnership act specify the mode of settlement of accounts on the dissolution of a partnership firm. It is as follows :

(1) First of all, the amount of loss, including the deficiency of Capital shall be paid out of profits, next out of Capital, and lastly, if necessary, will be realised from the partners in their profit sharing ratio.

(2) Amount realised from the sale of the assets of the firm (including any sum contributed by the partners), shall be applied in the following manner and order :

(I) First of all, outside debts of the firm will be paid.

(II) Out of the remaining amount, the loans advanced by partners will be paid off.

(III) Thereafter the balance of partners Capital Accounts will be returned.

(IV) If some amount remains, it will be divided among the partners in their profit sharing ratio.

Payment of Firm Debts and Private Debts (Sec. 49)

Firm's Debts : Debts which the firm owes to outsiders are called 'Firm's debts'.

Private Debts : Debts which a partner owes in his personal capacity are called 'Private debts'.

Following provisions apply for payment of firm's debts and private debts :

(*i*) Amount realised from the sale of the assets of the firm is first used to pay off firm debts and if there is any surplus available, it is distributed among the partners.

(*ii*) Amount realised from the sale of private estate of partners will be used first to pay the private debts of the partners, and if there is any surplus available, it will be used in paying off the firm's debts.

Distinction between 'Firm's Debts' and 'Private Debts'

	Basis	Firm's Debts	Private Debts
1.	**Meaning**	Firm's debts refer to the debts payable by the firm to outsiders.	Private debts refer to the debts payable by a partner in his personal capacity.
2.	**Who is Liable?**	For firm's debts, all partners are liable jointly and severally.	For private debts, only the concerned partner is liable personally.
3.	**Application of Firm's Property**	Firm's property is applied first towards payment of firm's debts.	Concerned partner's share in excess of firm's property over firm's debts can be applied towards payment of his private debts.
4.	**Application of Private Property**	Surplus of partner's private property over his private debts can be applied towards payment of firm's debts.	Private property is applied first towards payment of private debts.

Accounting Procedure on Dissolution of Firm

In order to close the books of the firm on dissolution the following accounts are opened in the order given below :

1. Realisation Account
2. Partner's Loan Accounts
3. Partner's Capital Accounts
4. Cash or Bank Account

1. **Realisation Account :—** A 'Realisation Account' is opened for disposing off all the assets of the firm and making payment to all the creditors. Realisation account is a nominal account and the object of such an account is to find out the profit or loss on realisation of assets and payment of liabilities. Entries in realisation account are made in the following manner :

(1) **For Closing Assets Accounts :—** All assets of the firm (except Cash and Bank balance) are transferred to this account **at book values.** Entry is :

Realisation A/c Dr.
  To Sundry Assets A/c
(Assets transferred to Realisation A/c at Book Values)

While transferring the assets to this account, the following points should be kept in mind :

(*i*) Only those assets which can be converted into Cash are transferred to this account. Fictitious assets such as accumulated losses like Dr. balance of P & L A/c and deferred revenue expenditure like Dr. balance of Advertisement Suspense A/c etc., are not included in the definition of assets and should not be transferred to Realisation A/c. Such accounts should be transferred to the Partner's Capital Accounts :

Partners' Capital A/cs Dr.
  To Profit & Loss A/c
  To Deferred Revenue Expenditure A/c
    (Such as Advertisement Suspense A/c)
(Balance of loss transferred to Partner's Capital A/cs in profit sharing ratio)

(*ii*) If there exists a provision against any asset, such as 'Provision for Bad and Doubtful Debts' or 'Provision for Depreciation' etc., the assets should be transferred to the Realisation A/c at its gross figure and such Provision A/c should be transferred to the Credit side of Realisation A/c. For example, if the total Debtors are ₹50,000 and the Provision for doubtful debts is ₹4,000, the entries will be :

(*a*) Realisation A/c	Dr.	50,000	
To Debtors A/c			50,000
(*b*) Provision for Doubtful Debts A/c	Dr.	4,000	
To Realisation A/c			4,000

Following entry is passed for the transfer of such provisions :

Provision for Bad debts A/c	Dr.
Provision for Depreciation A/c	Dr.
Machinery Replacement Reserve A/c	Dr.
Investment Fluctuation Fund A/c	Dr.
To Realisation A/c	
(Various reserves and provisions transferred to Realisation A/c)	

(*iii*) Cash and Bank balance are not transferred to realisation account.

(*iv*) Assets are always transferred to the realisation account at book values.

(2) **For Closing Liabilities Accounts :**

Sundry Liabilities A/c	Dr.
To Realisation A/c	
(Transfer of sundry liabilities to Realisation A/c)	

Following points should be kept in mind while passing the above entry :

(*i*) Only those liabilities which relate to third parties are transferred to Realisation A/c such as, Creditors, Bills Payable, other Outside Loans, Provident Fund, Outstanding Expenses, Partner's Wife Loan etc.

(*ii*) Partner's Loan Accounts too are not transferred to realisation account. Partner's Loan Accounts are prepared and paid off separately. This is because partner's loan is to be paid after payment of outside liabilities but before payment of partner's capitals.

(*iii*) Undistributed profits such as General Reserve, Reserve Fund, Credit balance of P & L A/c are also not transferred to Realisation A/c. These accounts are transferred to Partner's Capital accounts in their profit sharing ratio. Following entry is passed :

General Reserve A/c	Dr.
Reserve Fund A/c	Dr.
Contingency Reserve A/c	Dr.
Profit & Loss A/c	Dr.
To Partner's Capital A/cs	
(Undistributed profits transferred to Capital A/cs)	

Workmen Compensation Reserve :

This reserve is created out of profits of the firm to meet the claim for compensation by workers. At the time of dissolution, this reserve is dealt with as follows :

(*i*) **In case, there is no liability against Workmen Compensation Reserve :** In such a case, the entire amount of Workmen Compensation Reserve is Credited to the Capital Accounts of partners in their profit sharing ratio. The Journal Entry is :

Workmen Compensation Reserve A/c	Dr.		
To Partner's Capital A/cs			

(*ii*) **In case, the amount of liability is less than the amount of Workmen Compensation Reserve :** Amount equal to liability is Credited to Realisation Account and the remaining amount is Credited to Partners' Capital Accounts in their profit sharing ratio. (Suppose Workmen Compensation Reserve is ₹20,000 and liability for claim is ₹8,000) : The Journal Entry is :

Workmen Compensation Reserve A/c	Dr.	20,000	
To Realisation A/c			8,000
To Partner's Capital A/cs			12,000

(*iii*) **In case, the amount of liability is equal to the amount of Workmen Compensation Reserve :** The amount of Workmen Compensation Reserve is Credited to Realisation Account. The Journal Entry is :

Workmen Compensation Reserve A/c	Dr.		
To Realisation A/c			

(*iv*) **In case, the amount of liability is more than the amount of Workmen Compensation Reserve :** The entire amount of Workmen Compensation Reserve is transferred to Realisation Account. (Suppose Workmen Compensation Reserve is ₹20,000 and liability for claim is ₹25,000). The Journal entry is :

Workmen Compensation Reserve A/c	Dr.	20,000	
To Realisation A/c			20,000

ILLUSTRATION 1.

Lavanya and Priya were partners sharing profits in the ratio of 2 : 1. Pass journal entries for the following transactions at the time of dissolution of firm :

(*i*) Workmen Compensation Reserve stood at ₹1,50,000 in the Balance Sheet and there was no liability towards Workmen Compensation.

(*ii*) Workmen Compensation Reserve stood at ₹1,50,000 in the Balance Sheet and liability in respect of it was ascertained at ₹90,000.

(*iii*) Workmen Compensation Reserve stood at ₹1,50,000 in the Balance Sheet and liability in respect of it was ascertained at ₹1,50,000.

(*iv*) Workmen Compensation Reserve stood at ₹1,50,000 in the Balance Sheet and liability in respect of it was ascertained at ₹2,00,000.

(*v*) There was no Workmen Compensation Reserve in the Balance Sheet and firm had to pay ₹40,000 as compensation to the workers.

SOLUTION:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
(i)	Workmen Compensation Reserve A/c	Dr.		1,50,000	
	To Lavanya's Capital A/c				1,00,000
	To Priya's Capital A/c				50,000
	(Workmen Compensation Reserve transferred to Partners' Capital Accounts in their profit-sharing ratio)				
(ii) (a)	Workmen Compensation Reserve A/c	Dr.		90,000	
	To Realisation A/c				90,000
	(Workmen Compensation Reserve to the extent of liability transferred to Realisation Account)				
(b)	Workmen Compensation Reserve A/c	Dr.		60,000	
	To Lavanya's Capital A/c				40,000
	To Priya's Capital A/c				20,000
	(Surplus of Workmen Compensation Reserve transferred to Partners' Capital Account in their profit- sharing ratio)				
(c)	Realisation A/c	Dr.		90,000	
	To Bank A/c				90,000
	(Payment of liability on account of Workmen Compensation)				
(iii) (a)	Workmen Compensation Reserve A/c	Dr.		1,50,000	
	To Realisation A/c				1,50,000
	(Workmen Compensation Reserve transferred to Realisation Account)				
(b)	Realisation A/c	Dr.		1,50,000	
	To Bank A/c				1,50,000
	(Payment of liability on account of Workmen Compensation)				
(iv) (a)	Workmen Compensation Reserve A/c	Dr.		1,50,000	
	To Realisation A/c				1,50,000
	(Workmen Compensation Reserve transferred to Realisation Account)				
(b)	Realisation A/c	Dr.		2,00,000	
	To Bank A/c				2,00,000
	(Payment of liability on account of Workmen Compensation)				
(v)	Realisation A/c	Dr.		40,000	
	To Bank A/c				40,000
	(Payment of liability on account of Workmen Compensation)				

(3) Entries for realisation of Assets : (Whether recorded or unrecorded)

(*i*) When assets are sold for cash :

Cash/Bank A/c Dr.
To Realisation A/c
(Assets sold for Cash)

(*ii*) When asset is taken away by one of the partners :

Partners' Capital A/c Dr.
To Realisation A/c
(Assets taken over by partner)

(*iii*) If an asset is given away to a Creditor in part or full payment of his dues, the agreed amount of the asset is deducted from the claim of the Creditor and the balance is paid to him. No entry is passed for the transfer of asset to the creditor.

For example, if the amount due to a Creditor is ₹1,00,000 and he agrees to take stock of the book value of ₹80,000 at ₹70,000 and the balance in Cash, the following entry is passed :

Realisation A/c	Dr.	30,000	
To Bank A/c			30,000

ISC Council's Instruction
If the question is silent about the realisation of an asset, it is assumed that the asset has not realised any amount.

(4) Entries of payment of Outside Liabilities : (Whether recorded or unrecorded)

(*i*) When Liabilities are paid in Cash :

Realisation A/c Dr.
To Cash/Bank A/c
(Liabilities paid in cash)

(*ii*) When any partner agrees to take over some liability :

Realisation A/c Dr.
To Partners' Capital A/c
(Partner agreed to pay a liability)

ISC Council's Instruction
If the question is silent about the payment of a liability, it has to be paid out in full.

(5) For payment of realisation expenses :

(*i*) When expenses are paid by the firm :

Realisation A/c Dr.
To Cash/Bank A/c
(Realisation expenses paid in cash)

(*ii*) When realisation expenses are paid by a partner on behalf of the firm :

Realisation A/c Dr.
To Partners' Capital A/c
(Realisation expenses paid by partner)

(*iii*) When the firm has agreed to pay a fixed amount to the partner towards realisation expenses and the partner has to bear the expenses :

Realisation A/c Dr.
To Partner's Capital A/c
(Remuneration allowed to the partner)

(*iv*) When realisation expenses are to be borne by the partner and the expenses are paid by the firm :

Partner's Capital A/c Dr.
To Cash/Bank A/c
(Realisation expenses paid on behalf of the partner)

(*v*) No entry will be passed if the expenses are to be borne and paid by the partner out of his pocket.

Note : If nothing is mentioned about the treatment of realisation expenses it is assumed that the firm has met the realisation expenses.

ILLUSTRATION 2.

Pass journal entries for the following transactions :

(*i*) Realisation expenses amounted to ₹5,000.

(*ii*) Realisation expenses amounted to ₹8,000 were paid by partner *X*.

(*iii*) Realisation expenses amounted to ₹10,000 were paid by the firm on behalf of a partner.

(*iv*) Realisation expenses amounted to ₹15,000 were paid by the firm. Mr. *X*, one of the partners, has to bear these expenses.

(*v*) Realisation expenses amounted to ₹20,000 were paid by the firm. ₹8,000 were to be borne by the firm and the balance by Maruti, a partner.

(*vi*) Dissolution expenses amounted to ₹20,000. ₹8,000 were to be borne by the firm and the balance by Maruti, a partner. The expenses were paid by Maruti.

(*vii*) Sudhir, a partner, was allowed a remuneration of ₹10,000 to carry out dissolution of the firm. He was to bear all expenses of realisation which amounted to ₹16,000 were paid by the firm.

(*viii*) Ravi, a partner, is allowed a remuneration of ₹15,000 for dissolution work and is to bear all expenses of realisation which amounted to ₹5,000 were paid by the firm.

(*ix*) Anil, a partner, is paid remuneration of ₹20,000 for dissolution work. Realisation expenses amounted to ₹7,500 were paid by the firm.

(*x*) Sunil, a partner, is paid remuneration of ₹25,000 for dissolution work. Realisation expenses amounted to ₹9,000 were paid by him.

(*xi*) Vijay, a partner, paid realisation expenses of ₹10,000 and these were to be borne by him.

SOLUTION: JOURNAL ENTRIES

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
(*i*)	Realisation A/c	Dr.		5,000	
	To Bank A/c				5,000
	(Payment of realisation expenses)				
(*ii*)	Realisation A/c	Dr.		8,000	
	To *X*'s Capital A/c				8,000
	(Realisation expenses paid by *X* on behalf of the firm)				
(*iii*)	Partner's Capital A/c	Dr.		10,000	
	To Bank A/c				10,000
	(Realisation expenses paid by the firm on behalf of the partner)				
(*iv*)	*X*'s Capital A/c	Dr.		15,000	
	To Bank A/c				15,000
	(Realisation expenses paid by the firm on behalf of the partner)				
(*v*)	Realisation A/c	Dr.		8,000	
	Maruti's Capital A/c	Dr.		12,000	
	To Bank A/c				20,000
	(Realisation expenses paid by the firm. Firm's share of expenses debited to Realisation Account and balance to Partner's Capital Account)				
(*vi*)	Realisation A/c	Dr.		8,000	
	To Maruti's Capital A/c				8,000
	(Realisation expenses paid by the partner on behalf of the firm)				
(*vii*)	Realisation A/c	Dr.		10,000	
	Sudhir's Capital A/c	Dr.		6,000	
	To Bank A/c				16,000
	(Remuneration allowed to the partner and excess expenses charged from him)				
(*viii*)	Realisation A/c	Dr.		15,000	
	To Ravi's Capital A/c				10,000
	To Bank A/c				5,000
	(Remuneration allowed to Ravi and expenses paid by the firm on his behalf)				
(*ix*)	Realisation A/c*	Dr.		27,500	
	To Anil's Capital A/c				20,000
	To Bank A/c				7,500
	(Remuneration allowed and expenses paid)				

(x)	Realisation A/c* Dr. To Sunil's Capital A/c (Remuneration allowed and expenses paid by him)		34,000	34,000
(xi)	No Entry			

*In Case (ix) and (x) partner is not liable to bear the expenses of realisation.

ILLUSTRATION 3.

Pass necessary journal entries on the dissolution of a partnership firm in the following cases :

(i) Dissolution expenses were ₹800.

(ii) Dissolution expenses ₹800 were paid by Prabhu, a partner.

(iii) Geeta, a partner, was appointed to look after the dissolution work, for which she was allowed a remuneration of ₹10,000. Geeta agreed to bear the dissolution expenses. Actual dissolution expenses ₹9,500 were paid by Geeta.

(iv) Janki, a partner, agreed to look after the dissolution work for a commission of ₹5,000. Janki agreed to bear the dissolution expenses. Actual dissolution expenses ₹5,500 were paid by Mohan, another partner, on behalf of Janki.

(v) A partner, Kavita, agreed to look after dissolution process for a commission of ₹9,000. She also agreed to bear the dissolution expenses. Kavita took over furniture of ₹9,000 for her commission. Furniture had already been transferred to realisation account.

(vi) A debtor, Ravinder, for ₹19,000 agreed to pay the dissolution expenses which were ₹18,000 in full settlement of his debt. *(C.B.S.E. 2017, Outside Delhi)*

SOLUTION : JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
(i)	Realisation A/c Dr. To Bank A/c (Payment of dissolution expenses)		800	800
(ii)	Realisation A/c Dr. To Prabhu's Capital A/c (Dissolution expenses paid by Prabhu on behalf of the firm)		800	800
(iii)	Realisation A/c Dr. To Geeta's Capital A/c (Remuneration allowed to Geeta for dissolution work)		10,000	10,000
(iv)	Janki's Capital A/c Dr. Realisation A/c Dr. To Mohan's Capital A/c (Expenses paid by Mohan on behalf of Janki and Commission allowed to Janki)		500 5,000	5,500
(v)	No Entry			
(vi)	No Entry			

(6) **For closing realisation account :**

(*i*) When realisation account discloses profit (in case credit side is more than the debit side) :

Realisation A/c Dr.
To Partners' Capital A/cs
(Transfer of profit on Realisation to Partners' Capital A/cs)

(*ii*) When realisation account discloses loss (in case debit side is more than the credit side) :

Partners' Capital A/cs Dr.
To Realisation A/c
(Transfer of loss on Realisation to Partners' Capital A/cs)

Dr. **Format of Realisation Account** Cr.

Particulars	₹	*Particulars*	₹
To All assets (excluding cash/ bank balance, fictitious assets, Dr. balance of P & L A/c, Dr. balance of partner's Capital/ Current Accounts, Loan to partner)		By All liabilities (excluding Cr. balance of P & L A/c, Reserves, Partner's Capital/ Current Accounts, Loan from Partners)	
To Bank/Cash A/c (Amount paid for discharging liabilities)		By Provision on any asset (such as provision for doubtful debts, provision for depreciation etc.)	
To Bank/Cash A/c (Amount paid for unrecorded liabilities)		By Bank/Cash A/c (Amount received on realisation of assets)	
To Bank/Cash A/c (Expenses on realisation)		By Bank/Cash A/c (Amount received from unrecorded assets)	
To Partner's Capital A/c (Liability taken over by a partner or any expenses paid by him or remuneration/commission payable to him)		By Partner's Capital A/c (Asset taken over by a partner) By Partner's Capital A/cs (For transferring loss on realisation)	
To Partner's Capital A/cs (For transferring profit on realisation)			

Distinction Between Revaluation Account and Realisation Account

No.	*Basis of difference*	*Revaluation Account*	*Realisation Account*
1.	**When Prepared**	This account is prepared on the admission, retirement or death of a partner.	This account is prepared on the dissolution of partnership firm.
2.	**Object of Preparation**	This account is prepared to make necessary adjustments in the value of assets and liabilities.	This account is prepared to find out the profit or loss on the sale of assets and repayment of liabilities.

3.	**Result**	Even after the preparation of revaluation account the firm continues to function, though with a changed relationship among the partners.	The firm comes to an end after preparation of this account.
4.	**Value of Assets and Liabilities Recorded**	Only the difference between the book values and revised values of assets and liabilities is recorded in this account.	Book value of assets and liabilities, the realised value of assets and the actual payment of liabilities is recorded in this account.
5.	**When Prepared**	This account may be required to be prepared many times during the life-time of a firm.	This account is prepared only once during the life-time of a firm.

2. Partner's Loan to the Firm :

Loan given by a partner to the Firm is not an outside liability. Hence, it is not transferred to Realisation Account and will be paid off after all the outside liabilities are paid in full. Also, it is not transferred to Capital Account, because it is paid before payment of partner's capitals.

Hence, Partner's Loan A/c is prepared separately just after Realisation Account and it is paid off by passing the following entry :

Partner's Loan A/c Dr.
To Cash/Bank A/c

Partners' Loan is to be paid after payment of outside liabilities but before payment of capitals of the partners. However, if the Capital Account of the partner from whom loan has been taken by the firm shows a Dr. Balance after all adjustments, his loan account will be transferred to the credit of his Capital Account to the extent of debit balance of Capital Account.

For example :

Give necessary journal entries for settlement of Partner's Loan at the time of dissolution of firm under the following alternative cases :

Case 1. Loan from Manoj (a partner) ₹1,00,000, Manoj's Capital Account Credit Balance ₹40,000.

Case 2. Loan from Manoj (a partner) ₹1,00,000, Manoj's Capital Account Debit Balance ₹70,000.

Case 3. Loan from Manoj (a partner) ₹1,00,000, Manoj's Capital Account Debit Balance ₹1,25,000,

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
Case 1	Manoj's Loan A/c	Dr.		1,00,000	
	To Bank A/c				1,00,000
	(Repayment of Manoj's loan)				

Case 2	Manoj's Loan A/c	Dr.	1,00,000	
	To Manoj's Capital A/c			70,000
	To Bank A/c			30,000
	(Manoj's loan adusted against debit balance of his Capital Account and balance repaid)			
Case 3	Manoj's Loan A/c	Dr.	1,00,000	
	Bank A/c	Dr.	25,000	
	To Manoj's Capital A/c			1,25,000
	(Balance in Manoj's loan transferred to his Capital Account and deficiency brought in)			

(3) **Partner's Capital Accounts :—** After the transfer of profit or loss on realisation, undistributed profits, reserves etc. to the Capital Accounts of the partners the balance of Capital Accounts are closed in the following manner :

(*i*) When a partner is required to bring in cash to clear off his debit balance, the entry will be :

Cash/Bank A/c Dr.
To Partner's Capital A/c
(Required cash brought in by the partner)

(*ii*) When a partner is paid the Credit balance of his account :

Partner's Capital A/c Dr.
To Cash/Bank A/c
(Excess cash paid to partner)

(4) **Cash or Bank Account :—** Opening balance of Cash and Bank and all the receipts are entered on the debit side of this account and all the payments are entered on the credit side of this account. This account must be prepared and closed last of all and the total of both the sides of this account must be equal. In this way this account also helps in the verification of the arithmetical accuracy of the accounts.

Note : If Cash balance and Bank balance both are given in the balance sheet, only one account, either a Cash account or a Bank account is prepared. If cash account is prepared, an entry is passed for withdrawing the Bank balance and if a Bank account is prepared, the Cash balance is deposited into the bank.

ISC Council's Instruction
Loan taken from a partner will be passed through Cash or Bank Account.
Loan given to a partner will be transferred (debited) to his Capital Account.

ILLUSTRATION 4.

A and *B* shared profits in the ratio of 3 : 2. Their balance sheet as at 31st March, 2022 was as follows :

Liabilities	₹	*Assets*		₹
Creditors	20,000	Cash at Bank		8,000
Loan from *A*	16,000	Debtors	40,000	
General Reserve	25,000	*Less* : Provision	1,800	38,200

Capitals :			Stock	54,800
A	1,20,000		Investments	20,000
B	90,000	2,10,000	Machinery	40,000
			Land & Buildings	1,00,000
			Loan to B	10,000
		2,71,000		2,71,000

Partners decide to dissolve the firm on the above date. Assets realised as follows : Stock ₹45,000; Machinery 20% less than book value, Debtors ₹35,000. Land and Buildings ₹30,000 more than the book value. *A* took over investments at an agreed value of ₹15,000.

Creditors agreed to accept 5% less. Expenses of realisation of assets amounted to ₹1,200. There was a typewriter in the firm, which was bought out of the firm's money, was not shown in the books of the firm. It is now sold for ₹5,000.

Prepare Journal entries and give necessary accounts.

SOLUTION :

JOURNAL ENTRIES

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2022 March 31	Realisation A/c	Dr.		2,54,800	
	To Debtors A/c				40,000
	To Stock A/c				54,800
	To Investments A/c				20,000
	To Machinery A/c				40,000
	To Land & Buildings A/c				1,00,000
	(Transfer of various assets except cash to realisation a/c, **at book values**)				
	Creditors A/c	Dr.		20,000	
	Provision for Doubtful Debts A/c	Dr.		1,800	
	To Realisation A/c				21,800
	(Outside liabilities and provision transferred to realisation a/c, **at book figures**)				
	General Reserve A/c	Dr.		25,000	
	To *A*'s Capital A/c				15,000
	To *B*'s Capital A/c				10,000
	(General Reserve credited to partner's capital accounts)				
	Bank A/c	Dr.		2,42,000	
	To Realisation A/c				2,42,000
	(Amount realised on sale of Assets :				
	Stock	45,000			
	Machinery	32,000			
	Debtors	35,000			
	Land & Buildings	1,30,000			
		2,42,000)			

	A's Capital A/c Dr. To Realisation A/c (Investments taken over by *A*)		15,000	15,000
	Realisation A/c Dr. To Bank A/c (Creditors paid at a discount of 5%)		19,000	19,000
	Realisation A/c Dr. To Bank A/c (Payment of realisation expenses)		1,200	1,200
	Bank A/c Dr. To Realisation A/c (Amount received on sale of Typewriter)		5,000	5,000
	A's Loan A/c Dr. To Bank A/c (Payment of *A*'s loan)		16,000	16,000
	B's Capital A/c Dr. To *B*'s Loan A/c (Loan given to *B* transferred to the debit of his Capital Account)		10,000	10,000
	Realisation A/c Dr. To *A*'s Capital A/c To *B*'s Capital A/c (Profit on realisation transferred to partner's capital accounts)		8,800	5,280 3,520
	A's Capital A/c Dr. *B*'s Capital A/c Dr. To Bank A/c (Final payment made to partners)		1,25,280 93,520	2,18,800

Ledger Accounts

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Debtors A/c		40,000	By Creditors A/c	20,000
To Stock A/c		54,800	By Provision for Doubtful Debts A/c	1,800
To Investments A/c		20,000	By Bank A/c (Assets realised)	2,42,000
To Machinery A/c		40,000	By *A*'s Capital A/c (Investments taken by *A*)	15,000
To Land & Buildings A/c		1,00,000	By Bank A/c (Sale of Typewriter)	5,000
To Bank A/c (Creditors paid)		19,000		
To Bank A/c (Expenses paid)		1,200		
To Profit on Realisation transferred to :				
A's Capital A/c $\frac{3}{5}$	5,280			
B's Capital A/c $\frac{2}{5}$	3,520	8,800		
		2,83,800		2,83,800

A's LOAN ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Bank A/c	16,000	By Balance b/d	16,000
	16,000		16,000

CAPITAL ACCOUNTS

Dr. Cr.

Particulars	A ₹	B ₹	Particulars	A ₹	B ₹
To Loan to B		10,000	By Balance b/d	1,20,000	90,000
To Realisation A/c (Investments taken)	15,000		By General Reserve	15,000	10,000
To Bank A/c (Final Payment)	1,25,280	93,520	By Realisation A/c (Profit)	5,280	3,520
	1,40,280	1,03,520		1,40,280	1,03,520

BANK ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Balance b/d	8,000	By Realisation A/c (Creditors paid)	19,000
To Realisation A/c (Sale of assets)	2,42,000	By Realisation A/c (Expenses paid)	1,200
To Realisation A/c (Sale of Typewriter)	5,000	By A's Loan A/c	16,000
		By A's Capital A/c	1,25,280
		By B's Capital A/c	93,520
	2,55,000		2,55,000

Notes : (1) In all the questions it is necessary to prepare various accounts in the following order :

(*a*) First of all, realisation account should be prepared.

(*b*) Secondly, if a partner has given any loan to the firm, Partner's Loan Account should be prepared.

(*c*) Thereafter Partner's Capital Accounts are prepared.

(*d*) Bank Account is prepared last of all.

Partner's Loan Account is prepared before Capital Accounts because at the time of dissolution Capitals are paid off only if any balance is left after payment of partner's loans.

(2) Assets are transferred to the realisation account on the values given in the balance sheet.

(3) Cash or Bank balance is not transferred to realisation account. A separate account is prepared for Cash and Bank.

ILLUSTRATION 5.

Diya and Riya were partners sharing profits and losses equally. On 31st March, 2016, the Balance Sheet of the firm was as follows :

BALANCE SHEET *as at 31st March, 2016*

Liabilities	₹	Assets	₹
Sundry Creditors	60,000	Cash	25,000

Riya's Loan	15,000	Debtors	42,000	
General Reserve	15,000	*Less* : Provision for		
Investment Fluctuation Fund	2,000	Doubtful Debts	6,000	36,000
Riya's Capital	30,000	Stock		12,000
Diya's Capital	10,000	Investments		18,000
		Plant and Machinery		39,000
		Diya's Loan		2,000
	1,32,000			1,32,000

Their firm was dissolved on above date and the assets and liabilities were settled as follows :

(*i*) The creditors were paid off by giving them the plant and machinery at a discount of 10% and the balance in cash.

(*ii*) Riya's loan was paid with interest of ₹500.

(*iii*) Debtors realised 10% less of the amount due from them.

(*iv*) Stock was taken over by Riya at ₹7,000.

(*v*) Investments realised 80% of their book value.

(*vi*) Realisation expenses ₹600 were paid by Diya.

You are required to prepare :

(*a*) Realisation Account.

(*b*) Riya's Loan Account and Diya's Loan Account

(*c*) Capital Accounts, and

(*d*) Bank Account.

(ISC Sample Paper, 2017)

SOLUTION :

Dr. REALISATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Debtors A/c	42,000	By Provisions for Doubtful		
To Stock A/c	12,000	Debts A/c		6,000
To Investments A/c	18,000	By Sundry Creditors A/c		60,000
To Plant and Machinery A/c	39,000	By Investment Fluctuation		
To Cash A/c (Creditors)		Fund A/c[1]		2,000
(₹60,000 – ₹35,100)	24,900	By Cash A/c (Assets Realised)		
To Riya's Loan A/c (Interest)	500	Debtors	37,800	
To Diya's Capital A/c (Expenses)	600	Investments	14,400	52,200
		By Riya's Capital A/c		
		(Stock taken)		7,000
		By Loss on Realisation		
		transferred to :		
		Diya's Capital A/c	4,900	
		Riya's Capital A/c	4,900	9,800
	1,37,000			1,37,000

RIYA'S LOAN ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Cash A/c	15,500	By Balance b/d	15,000
		By Realisation A/c (Interest)	500
	15,500		15,500

DIYA'S LOAN ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Balance b/d	2,000	By Diya's Capital A/c	2,000

PARTNER'S CAPITAL ACCOUNTS

Dr. Cr.

Particulars	Riya	Diya	Particulars	Riya	Diya
	₹	₹		₹	₹
To Diya's Loan A/c		2,000	By Balance b/d	30,000	10,000
To Realisation A/c (Stock taken)	7,000		By Realisation A/c (Expenses paid)		600
To Realisation A/c (Loss)	4,900	4,900	By General Reserve A/c	7,500	7,500
To Cash A/c (Final Payment)	25,600	11,200			
	37,500	18,100		37,500	18,100

CASH ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Balance b/d	25,000	By Realisation A/c (Creditors paid)	24,900
To Realisation A/c (Assets realised)	52,200	By Riya's Loan A/c	15,500
		By Riya's Capital A/c	25,600
		By Diya's Capital A/c	11,200
	77,200		77,200

Notes : (1) Investment Fluctuation Fund is transferred to the Cr. side of realisation A/c, but it is not to be paid, as it is not the actual liability.

It should be noted that :

Investment Fluctuation Fund will be transferred to Realisation A/c only if investments are appearing on the Assets side, Otherwise, it will be Credited to Capital Accounts.

Treatment of Goodwill :

Treatment of goodwill is very easy in case of dissolution of a firm. It may be summarised as under :

(*i*) If goodwill is already appearing in the Balance Sheet, it is treated like any other asset, and is transferred to the Realisation Account at the value given in balance sheet. Following entry is passed for it :

Realisation A/c Dr.

To Goodwill A/c

(*ii*) If goodwill is not appearing in the Balance Sheet, the above mentioned entry will not be passed.

(*iii*) When some amount is realised for goodwill :

Cash/Bank A/c Dr.
To Realisation A/c

(*iv*) If goodwill is taken over by any of the partners :

Partner's Capital A/c Dr.
To Realisation A/c

Note : If the question is silent about the realisation of goodwill, it is assumed that goodwill has not realised any amount.

ILLUSTRATION 6.

X, *Y* and *Z* were partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. Following was the Balance Sheet at the date of dissolution :

Liabilities	₹	*Assets*		₹
Creditors	18,500	Bank balance		1,000
Mrs. *X*'s Loan	5,000	Debtors	15,000	
X's Loan	8,000	*Less* : Provision	1,000	14,000
Workmen Compensation Reserve	30,000	Stock		80,000
Investment Fluctuation Fund	7,500	Investments		20,000
Capital Accounts :		Plant		75,000
X	60,000	Goodwill		35,000
Y	56,000			
Z	40,000			
	2,25,000			2,25,000

Following transactions took place :

I. *X* took over the investments at 25% more than the book value.

II. *Y* took over debtors amounting to ₹5,000 at ₹4,000. Remaining debtors realised 75% of their book value.

III. Stock is sold for ₹59,000 and plant is sold for ₹40,000.

IV. Expenses of realisation amounted to ₹1,000. It was also found that there is a liability for ₹8,000 for damages, which also had to be paid. Prepare necessary accounts.

SOLUTION :

Dr. REALISATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Debtors	15,000	By Provision for Doubtful Debts	1,000
To Stock	80,000	By Creditors	18,500
To Investments	20,000	By Mrs. *X*'s Loan	5,000
To Plant	75,000	By Investment Fluctuation Fund	7,500
To Goodwill	35,000	By Bank A/c (assets realised)	

To Bank A/c (expenses)		1,000	Debtors (75% of ₹10,000)	7,500	
To Bank A/c (damages)		8,000	Stock	59,000	
To Bank A/c :			Plant	40,000	1,06,500
Creditors	18,500		By X's Capital A/c (Investments taken)		25,000
Mrs. X's Loan	5,000	23,500	By Y's Capital A/c (Debtors taken)		4,000
			By Loss transferred to :		
			X's Capital A/c	45,000	
			Y's Capital A/c	30,000	
			Z's Capital A/c	15,000	90,000
		2,57,500			2,57,500

Dr. X's LOAN ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Bank A/c	8,000	By Balance b/d	8,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	X	Y	Z	Particulars	X	Y	Z
	₹	₹	₹		₹	₹	₹
To Realisation A/c (Assets taken)	25,000	4,000		By Balance b/d	60,000	56,000	40,000
To Realisation A/c (Loss)	45,000	30,000	15,000	By Workmen Compensation Reserve	15,000	10,000	5,000
To Bank A/c (Final payment)	5,000	32,000	30,000				
	75,000	66,000	45,000		75,000	66,000	45,000

Dr. BANK ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance b/d	1,000	By Realisation A/c (expenses)	1,000
		By Realisation A/c (damages)	8,000
To Realisation A/c (Sale of assets)	1,06,500	By Realisation A/c (liabilities)	23,500
		By X's Loan A/c	8,000
		By X Capital A/c	5,000
		By Y Capital A/c	32,000
		By Z Capital A/c	30,000
	1,07,500		1,07,500

Note : (1) If nothing is mentioned in the question about the payment of outside liabilities, it is assumed that these are paid in full. Hence Creditors and Mrs. X's Loan are to be paid in full in this question. Following entry will be passed for their payment :

Realisation A/c Dr.
To Bank A/c

Note : (2) Goodwill appears in the Balance Sheet. It will be treated like any other asset and is transferred to the debit of realisation account. It will be assumed that goodwill has not realised any amount.

ILLUSTRATION 7.

Following was the Balance Sheet of *D, G* and *T* as at 29.2.2020 :

Liabilities		*Amount*	*Assets*	*Amount*
		₹		₹
Creditors		50,000	Bank	26,000
Bills Payable		10,000	Debtors	30,000
G's Loan		8,000	Stock	20,000
R's Loan		12,000	Furniture	15,000
Workmen Compensation Reserve		26,000	Land and Building	2,45,000
Capitals :			*G*'s Capital	20,000
D	1,00,000			
T	1,50,000	2,50,000		
		3,56,000		3,56,000

The firm was dissolved on the above date on the following terms :

(*i*) Debtors realized ₹28,000; and creditors and bills payable were paid at a discount of 10%.

(*ii*) Stock was taken over by *T* for ₹15,000 and furniture was sold to *N* for ₹12,000.

(*iii*) Land and building was sold for ₹2,80,000.

(*iv*) *R*'s loan was paid by a cheque for the same amount.

(*v*) There was an unrecorded asset of ₹1,50,000 which was sold for ₹1,00,000.

(*vi*) Compensation to workmen paid by the firm amounted to ₹20,000.

Prepare Realisation Account, Bank Account and Capital Accounts of *D, G* and *T*.

SOLUTION :

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	*Particulars*		₹
To Debtors		30,000	By Creditors		50,000
To Stock		20,000	By Bills Payable		10,000
To Furniture		15,000	By *R*'s Loan		12,000
To Land and Building		2,45,000	By Workmen Compensation Reserve A/c		20,000
To Bank A/c :			By Bank A/c (assets realised)		
Creditors	45,000		Debtors	28,000	
Bills Payable	9,000		Furniture	12,000	
R's Loan	12,000	66,000	Land and Building	2,80,000	3,20,000
To Bank A/c (Workmen Compensation paid off)		20,000	By *T*'s Capital A/c (Stock Taken)		15,000
To Profit Transferred to :			By Bank A/c (Unrecorded Asset)		1,00,000

D's Capital A/c	43,667			
G's Capital A/c	43,667			
T's Capital A/c	43,666	1,31,000		
		5,27,000		5,27,000

Dr. **G's LOAN ACCOUNT** Cr.

Particulars	₹	*Particulars*	₹
To Bank A/c	8,000	By Balance b/d	8,000
	8,000		8,000

Dr. **CAPITAL ACCOUNTS** Cr.

Particulars	D	G	T	*Particulars*	D	G	T
	₹	₹	₹		₹	₹	₹
To Balance b/d	—	20,000	—	By Balance b/d	1,00,000	—	1,50,000
To Realisation A/c (Stock taken	—	—	15,000	By Workmen Compensation Reserve	2,000	2,000	2,000
To Bank A/c	1,45,667	25,667	1,80,666	By Realisation A/c (Profit)	43,667	43,667	43,666
	1,45,667	45,667	1,95,666		1,45,667	45,667	1,95,666

Dr. **BANK ACCOUNT** Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	26,000	By Realisation A/c (Liabilities paid)	66,000
To Realisation A/c (Sale of Assets)	3,20,000	By Realisation A/c (Workmen Compensation paid)	20,000
To Realisation A/c (Unrecorded Asset)	1,00,000	By G's Loan A/c	8,000
		By D's Capital A/c	1,45,667
		By G's Capital A/c	25,667
		By T's Capital A/c	1,80,666
	4,46,000		4,46,000

Working Notes :

(1) Entry for Workmen Compensation Reserve :

Workmen Compensation Reserve A/c	Dr.	26,000	
To Realisation A/c			20,000
To D's Capital A/c			2,000
To G's Capital A/c			2,000
To T's Capital A/c			2,000

(2) Entry for Payment of Compensation :

Realisation A/c	Dr.	20,000	
To Bank A/c			20,000

(3) G's Capital Account shows a Cr. balance of ₹25,667 after all adjustments. Hence his loan has been paid off separately. On the contrary, if his Capital Account (after all adjustments) had shown a Dr. balance, his Loan Account would have been transferred to his Capital Account to the extent of debit balance of Capital Account and the balance, if any, in his Loan Account would have been paid off.

ISC Council's Instruction	
(*i*)	**Bank Overdraft** is not to be transferred to Realisation Account. It is a negative bank balance to be shown on the Cr. side of Bank Account.
(*ii*)	**Bank Loan** must be transferred to Realisation Account.

ILLUSTRATION 8.

A, *B* and *C* are partners sharing profits and losses in the ratio of 2 : 2 : 1. They agreed to dissolve the firm. The Balance Sheet of the firm at that date was as follows :

Liabilities		₹	*Assets*	₹
Bank Overdraft		4,000	Debtors	40,000
Creditors		30,000	Stock	50,000
B/P		6,000	Furniture	2,000
B's Wife Loan		10,000	Computer	8,000
Capitals :	*A*	70,000	Fixed Assets	41,000
	B	70,000	Prepaid Expenses	1,000
			Profit & Loss A/c	40,000
			C's Capital	8,000
		1,90,000		1,90,000

1. Assets realised as follows : Stock ₹32,000; Fixed Assets ₹45,000 and full amount was received from Debtors.
2. *A* agreed to take over furniture at ₹1,600 and also agrees to make the payment of B/P.
3. *B* agreed to discharge his wife's loan.
4. There was an unrecorded asset of ₹10,000, which was taken over by *C* at ₹7,000.
5. A B/R for ₹5,000 was received from a customer Mohan and the bill was discounted from the bank. Mohan became insolvent and 60 paise per rupee has been received from his estate.
6. Creditors were paid at a discount of ₹1,500.

Prepare necessary accounts.

SOLUTION :

Working Notes :

(1) Entry for Furniture taken away by *A* :

A	Dr.	1,600	
To Realisation A/c			1,600

Entry for *A* agreeing to discharge the liability of B/P :

Realisation A/c	Dr.	6,000	
To *A*			6,000

(2) Entry for *B* agreeing to discharge his wife's loan :

Realisation A/c	Dr.	10,000	
To *B*			10,000

(3) Entry for an unrecorded asset taken over by *C* :

C	Dr.	7,000	
To Realisation A/c			7,000

(4) Entries for B/R received from Mohan :

(*i*) Bank A/c	Dr.	3,000	
To Realisation A/c			3,000
(*ii*) Realisation A/c	Dr.	5,000	
To Bank A/c			5,000

(5) It will be assumed that Computer has not realised any amount.

(6) *C*'s Capital account shows a debit balance (*i.e.*, deficit). It will be assumed that he brings in necessary cash to clear off his debit balance, unless it is specifically mentioned in the question that he has become insolvent.

Dr. REALISATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Debtors	40,000	By Creditors		30,000
To Stock	50,000	By B/P		6,000
To Furniture	2,000	By *B*'s Wife Loan		10,000
To Computer	8,000	By Bank A/c (Sale of assets)		1,17,000
To Fixed Assets	41,000	By Bank A/c (Recovery from B/R dishonoured)		3,000
To Prepaid Expenses	1,000	By *A*'s Capital (Furniture)		1,600
To *A*'s Capital (B/P)	6,000	By *C*'s Capital (Unrecorded asset)		7,000
To *B*'s Capital (Wife Loan)	10,000	By Loss transferred to :		
To Bank (payment for bill discounted)	5,000	*A*'s Capital A/c	6,760	
To Bank (Creditors)	28,500	*B*'s Capital A/c	6,760	
		C's Capital A/c	3,380	16,900
	1,91,500			1,91,500

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Bal. b/d			8,000	By Bal. b/d	70,000	70,000	

To P & L A/c	16,000	16,000	8,000	By Realisation (B/P)	6,000		
To Realisation (Furniture)	1,600			By Realisation (Wife Loan)		10,000	
To Realisation (Asset)			7,000	By Bank A/c (Cash brought in)			26,380
To Realisation (Loss)	6,760	6,760	3,380				
To Bank A/c (Final payment)	51,640	57,240					
	76,000	80,000	26,380		76,000	80,000	26,380

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Realisation A/c	1,17,000	By Bal. b/d	4,000
To Realisation A/c (Recovery from B/R dishonoured)	3,000	By Realisation (payment for bill discounted)	5,000
To C's Capital A/c (Cash brought in)	26,380	By Realisation (Creditors)	28,500
		By *A*'s Capital A/c	51,640
		By *B*'s Capital A/c	57,240
	1,46,380		1,46,380

ILLUSTRATION 9.

Ashish and Kanav were partners in a firm sharing profits and losses in the ratio of 3 : 2. On 31st March, 2018 their Balance Sheet was as follows :

BALANCE SHEET OF ASHISH AND KANAV
as at 31st March, 2018

Liabilities		₹	*Assets*	₹
Trade Creditors		42,000	Bank	35,000
Employees' Provident Fund		60,000	Stock	24,000
Mrs. Ashish's Loan		9,000	Debtors	19,000
Kanav's Loan		35,000	Furniture	40,000
Workmen's Compensation Reserve		20,000	Plant	2,10,000
Investment Fluctuation Reserve		4,000	Investments	12,000
Capitals :			Profit and Loss Account	10,000
Ashish	1,20,000			
Kanav	80,000	2,00,000		
		3,70,000		3,70,000

On the above date they decided to dissolve the firm.

(*i*) Ashish agreed to take over furniture at ₹38,000 and pay off Mrs. Ashish's loan.

(*ii*) Debtors realised ₹18,500 and plant realised 10% more.

(*iii*) Kanav took over 40% of the stock at 20% less than the book value. Remaining stock was sold at a gain of 10%.

(*iv*) Trade creditors took over investments in full settlement.

(*v*) Kanav agreed to take over the responsibility of completing dissolution at an agreed remuneration of ₹12,000 and to bear realization expenses. Actual expenses of realization amounted to ₹8,000.

Prepare Realisation Account. *(C.B.S.E. 2019, Rajasthan)*

SOLUTION :

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	*Particulars*		₹
To Sundry Assets :			By Sundry Liabilities :		
Stock	24,000		Trade Creditors	42,000	
Debtors	19,000		Employee's Provident Fund	60,000	
Furniture	40,000				
Plant	2,10,000		Mrs. Ashish's Loan	9,000	1,11,000
Investments	32,000	3,25,000	By Investment Fluctuation Reserve		4,000
To Ashish's Capital A/c (Mrs. Ashish's Loan)		9,000	By Ashish's Capital A/c (Furniture)		38,000
To Kanav's Capital A/c (Remuneration)		12,000	By Bank A/c :		
To Bank A/c (Payment made):			Debtors	18,500	
Employee's Provident Fund		60,000	Plant	2,31,000	
To Partner's Capital A/cs : (Gain)			Stock	15,840	2,65,340
Ashish	12,012		By Kanav's Capital A/c (Stock)		7,680
Kanav	8,008	20,020			
		4,26,020			4,26,020

Working Notes :

(*i*) Partner's Loan (Kanav's Loan) A/c will be prepared separately.

(*ii*) Workmen's Compensation Reserve will be transferred to Partner's Capital Accounts.

(*iii*) There will be no entry of taking over of Investments by Trade Creditors.

ILLUSTRATION 10.

The following is the Balance Sheet of *A* and *B* as at 31st March, 2022 :

Liabilities	₹	*Assets*		₹
Sundry Creditors	30,000	Cash in Hand		500
Bills Payable	8,000	Cash at Bank		8,000
Mrs. *A*'s Loan	5,000	Stock in Trade		5,000
Mrs. *B*'s Loan	10,000	Investments		10,000
General Reserve	10,000	Debtors	20,000	
Investment Fluctuation Fund	1,000	*Less* : Provision	2,000	18,000
A's Capital	10,000	Plant		20,000
B's Capital	10,000	Building		15,000

		Goodwill	4,000
		Advertisement Suspense A/c	3,500
	84,000		84,000

The firm was dissolved on 31st March, 2022 on the following terms :

(*a*) *A* promised to pay Mrs. *A*'s loan and took away stock in-trade at ₹4,000.

(*b*) *B* took away half of the investments at 10% discount.

(*c*) Debtors realized ₹19,000 (including bad debts recovered ₹6,000).

(*d*) Creditors and bills payable were due on an average basis of one month after 31st March, but they were paid immediately on 31st March at 6% discount, p.a.

(*e*) Plant realized ₹25,000, building ₹40,000, goodwill ₹6,000 and remaining investments at ₹4,500.

(*f*) There was an old typewriter in the firm which had been written off completely from the books, it was estimated to realize ₹300, it was taken away by *B* at this estimated price.

You are required to prepare the (*a*) realisation A/c (*b*) partners' capital A/cs and (*c*) bank A/c to close books of the firm.

SOLUTION :

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	Particulars		₹
To Stock in Trade		5,000	By Provision for Doubtful Debts		2,000
To Investments		10,000	By Sundry Creditors		30,000
To Debtors		20,000	By Bills Payable		8,000
To Plant		20,000	By Mrs. *A*'s Loan		5,000
To Building		15,000	By Mrs. *B*'s Loan		10,000
To Goodwill		4,000	By Investment Fluctuation Fund		1,000
To *A*'s Capital (Mrs. *A*'s loan)		5,000	By *A*'s Capital (Stock in trade)		4,000
To Bank (Sundry Creditors) (Note 1)		29,850	By *B*'s Capital (half of investments at 10% discount)		4,500
To Bank (Bills Payable) (Note 1)		7,960	By Bank :		
To Bank (Mrs. *B*'s Loan)		10,000	Debtors	19,000	
To Profit transferred to :			Plant	25,000	
A's Capital A/c	16,245		Building	40,000	
B's Capital A/c	16,245	32,490	Goodwill	6,000	
			Investments	4,500	94,500
			By *B*'s Capital (unrecorded asset)		300
		1,59,300			1,59,300

Dr. PARTNER'S CAPITAL ACCOUNT Cr.

Particulars	*A*	*B*	Particulars	*A*	*B*
	₹	₹		₹	₹
To Advertisement Suspense A/c	1,750	1,750	By Balance b/d	10,000	10,000
			By General Reserve	5,000	5,000

To Realisation (Stock in trade)	4,000	—	By Realisation (Mrs. *A*'s Loan)	5,000	—
To Realisation (Investments)	—	4,500	By Realisation (Profit)	16,245	16,245
To Realisation (Unrecorded asset)	—	300			
To Bank	30,495	24,695			
	36,245	31,245		36,245	31,245

Dr. BANK ACCOUNT Cr.

Particulars		₹	*Particulars*	₹
To Balance b/d		8,000	By Realisation (Sundry Creditors)	29,850
To Cash (Cash balance deposited into bank)		500	By Realisation (Bills Payable)	7,960
To Realisation :			By Realisation (Mrs. *B*'s Loan)	10,000
Debtors	19,000		By *A*'s Capital A/c	30,495
Plant	25,000		By *B*'s Capital A/c	24,695
Building	40,000			
Goodwill	6,000			
Investments	4,500	94,500		
		1,03,000		1,03,000

Note (1) Calculation of discount on Creditors and Bills Payable :

Creditors — $30,000 \times \frac{1}{12} \times \frac{6}{100} = ₹150$

Bills Payable — $8,000 \times \frac{1}{12} \times \frac{6}{100} = ₹\ 40$

ILLUSTRATION 11.

Following is the Balance Sheet of *X* and *Y*, who share profits and losses in the ratio of 4 : 1, as at 31st March, 2022 :

Liabilities	₹	*Assets*		₹
Sundry Creditors	8,000	Bank		20,000
Bank Overdraft	6,000	Debtors	17,000	
X's Brother's Loan	8,000	*Less* : Provision	2,000	15,000
Y's Loan	3,000	Stock		15,000
Investment Fluctuation Fund	5,000	Investments		25,000
Capital :		Furniture		6,000
X	50,000	Buildings		19,000
Y	40,000	Goodwill		10,000
		Profit and Loss A/c		10,000
	1,20,000			1,20,000

The firm was dissolved on the above date and the following arrangements were decided upon :

(*i*) *X* agreed to pay off his brother's Loan.

(*ii*) Debtors of ₹5,000 proved bad.

(iii) Other assets realised — Investments 20% less; and Goodwill at 60%.

(iv) One of the creditors of ₹5,000 was paid only ₹3,000.

(v) Buildings were auctioned for ₹30,000 and the auctioneer's commission amounted to ₹1,000.

(vi) Y took over part of stock at ₹4,000 (being 20% less than the book value). Balance stock realised 50%.

(vii) Realisation expenses amounted to ₹2,000.

Prepare :

(i) Realisation Acount

(ii) Partners' Capital Accounts, and

(iii) Bank Account.

SOLUTION:

Dr. REALISATION ACCOUNT Cr.

Particulars	₹	Particulars		₹
To Debtors	17,000	By Provision for Doubtful Debts		2,000
To Stock	15,000	By Sundry Creditors		8,000
To Investments	25,000	By X's Brother's Loan		8,000
To Furniture	6,000	By Investment Fluctuation Fund		5,000
To Buildings	19,000	By Bank :		
To Goodwill	10,000	Debtors (₹17,000		
To X's Capital A/c		– ₹5,000)	12,000	
(X's Brother's loan)	8,000	Investments	20,000	
To Bank (Creditors paid)	6,000	Goodwill	6,000	
To Bank (Expenses)	2,000	Buildings	29,000	
		Stock (Note 1)	5,000	72,000
		By Y's Capital : (Stock)		4,000
		By Loss Transferred to :		
		X's Capital A/c	7,200	
		Y's Capital A/c	1,800	9,000
	1,08,000			1,08,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	X	Y	Particulars	X	Y
	₹	₹		₹	₹
To Profit and Loss A/c	8,000	2,000	By Balance b/d	50,000	40,000
To Realisation A/c			By Realisation A/c		
(Stock Taken)		4,000	(Brother's Loan)	8,000	
To Realisation A/c (Loss)	7,200	1,800			
To Bank A/c					
(Final Payment)	42,800	32,200			
	58,000	40,000		58,000	40,000

BANK ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Balance b/d	20,000	By Balance b/d (Bank Overdraft)	6,000
To Realisation A/c		By Realisation A/c (Creditors)	6,000
(Assets realised)	72,000	By Realisation A/c (Expenses)	2,000
		By Y's Loan A/c	3,000
		By X's Capital A/c	42,800
		By Y's Capital A/c	32,200
	92,000		92,000

Notes :

(1) *Y* has taken over stock at ₹4,000 which is 80% of the book value of such stock.

Thus, if stock is taken at ₹80, book value = ₹100

if stock is taken at ₹4,000, book value $= \frac{100}{80} \times 4{,}000 =$ ₹5,000

Book Value of remaining stock = ₹15,000 – ₹5,000 = ₹10,000

Amount realised from balance stock $= 10{,}000 \times \frac{50}{100} =$ ₹5,000

(2) Since the question is silent about the realisation of furniture, it is assumed that furniture has realised nothing.

ILLUSTRATION 12.

A, *B* and *C* are three partners sharing profits in the ratio of 3 : 1 : 1. On 31st March, 2022, they decided to dissolve their firm. At that date their balance sheet was as under:—

Liabilities		₹	*Assets*		₹
Creditors		60,000	Bank		52,000
Loan		15,000	Cash		10,000
Workmen Compensation Reserve		30,000	Debtors	2,42,000	
Capital A/cs :			*Less* : Provision for Bad Debts	12,000	2,30,000
A	2,75,000		Stock in Trade		78,000
B	1,00,000		Furniture		10,000
C	70,000	4,45,000	Sundry Assets		1,70,000
		5,50,000			5,50,000

It is agreed that:—

(*i*) *A* is to take over Furniture at ₹8,000 and Debtors amounting to ₹2,00,000 at ₹1,82,000; the Creditors of ₹60,000 to be paid by him at this figure.

(*ii*) *B* is to take over all the Stock in Trade at ₹70,000 and some of the Sundry Assets at ₹72,000 (being 10% less than book value).

(*iii*) *C* is to take over the remaining Sundry Assets at 90% of the book value, less ₹1,000 as discount and assume the responsibility for the discharge of the loan together with accrued interest of ₹300 which has not been recorded in the books.

(*iv*) The expenses of dissolution were ₹2,700. The remaining debtors were sold to a debt collecting agency for 50% of the book value.

(v) ₹40,000 had to be paid for Workmen Compensation.

Prepare necessary accounts to close the books of the firm.

SOLUTION:

REALISATION ACCOUNT

Dr. Cr.

Particulars		₹	Particulars		₹
To Debtors		2,42,000	By Provision for Bad Debts A/c		12,000
To Stock-in-Trade		78,000	By Creditors A/c		60,000
To Furniture		10,000	By Loan A/c		15,000
To Sundry Assets		1,70,000	By Workmen Compensation Reserve		30,000
To *A*'s Capital A/c (Creditors taken)		60,000	By *A*'s Capital A/c :		
To *C*'s Capital A/c			Furniture	8,000	
Loan	15,000		Debtors	1,82,000	1,90,000
Accrued Interest	300	15,300	By *B*'s Capital A/c:		
To Bank A/c (Expenses)		2,700	Stock in Trade	70,000	
To Bank A/c (Payment of Workmen Compensation)		40,000	Sundry Assets	72,000	1,42,000
			By *C*'s Capital A/c : Sundry Assets(2)		80,000
			By Bank A/c (Debtors)(3)		21,000
			By Loss transferred to :		
			A's Capital A/c 3/5	40,800	
			B's Capital A/c 1/5	13,600	
			C's Capital A/c 1/5	13,600	68,000
		6,18,000			6,18,000

CAPITAL ACCOUNTS

Dr. Cr.

Particulars	*A*	*B*	*C*	Particulars	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Realisation A/c (Assets taken)	1,90,000	1,42,000	80,000	By Balance b/d	2,75,000	1,00,000	70,000
To Realisation A/c (Loss)	40,800	13,600	13,600	By Realisation A/c (Liabilities taken)	60,000	—	15,300
To Bank A/c (Final Payment)	1,04,200	—	—	By Bank A/c (Deficit brought in Cash)	—	55,600	8,300
	3,35,000	1,55,600	93,600		3,35,000	1,55,600	93,600

BANK ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Balance b/d	52,000	By Realisation A/c (Expenses)	2,700
To Cash A/c (Cash balance deposited into bank)	10,000	By Realisation A/c (Payment of Workmen Compensation)	40,000
To Realisation A/c (Debtors)	21,000	By *A*'s Capital A/c	1,04,200
To *B*'s Capital A/c	55,600		

To C's Capital A/c		8,300		
		1,46,900		1,46,900

Note : (1) *B* has taken over some of the Sundry Assets at an agreed value of ₹72,000. This amount is 90% of the book value of Sundry Assets taken over by *B*.

Thus, if agreed value is 90, book value = ₹100

if agreed value is 72,000, book value = $\frac{100}{90} \times 72{,}000 = 80{,}000$

(2) Remaining Sundry Assets have been taken over by *C*. Book value of the remaining Sundry Assets = ₹1,70,000 – ₹80,000 = ₹90,000.

C takes over these Sundry Assets at $90{,}000 \times \frac{90}{100} = 81{,}000$ *less* 1,000 = ₹80,000

(3) Out of total Debtors of ₹2,42,000, *A* has taken over Debtors of ₹2,00,000. Hence, the balance is ₹42,000 on which 50% or ₹21,000 are received.

ILLUSTRATION 13.

A and *B* were partners in a firm sharing profits in the ratio of 3 : 2. On 31.3.2022 the Balance Sheet of the firm was as follows :

BALANCE SHEET OF *A* AND *B as at 31.3.2022*

Liabilities		₹	*Assets*	₹
Capitals :			Building	2,40,000
A	3,00,000		Furniture	1,75,000
B	2,00,000	5,00,000	Debtors	80,000
Sundry Creditors		97,000	Stock	75,000
A's Loan		20,000	Cash	47,000
		6,17,000		6,17,000

The firm was dissolved on 1.4.2022 and the assets and liabilities were settled as following :

(*i*) Building was taken over by the creditors as their full and final payment;

(*ii*) *A* accepted an unrecorded asset of ₹25,000 in full settlement of his loan.

(*iii*) Furniture was taken over by *B* for cash payment at 5% less than the book value;

(*iv*) Debtors were collected by a debt collection agency at a cost of ₹5,000;

(*v*) Stock realised ₹70,500.

(*vi*) *B* agreed to bear all realisation expenses. For this service *B* is to be allowed ₹500. Actual expenses on realisation ₹1,000 were paid by *B*.

Pass necessary journal entries for dissolution of the firm.

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
1.4.2022	Realisation A/c	Dr.		5,70,000	
	To Building A/c				2,40,000
	To Furniture A/c				1,75,000
	To Debtors A/c				80,000
	To Stock A/c				75,000
	(Assets transferred to Realisation A/c on dissolution)				

1.4.2022	Sundry Creditors A/c To Realisation A/c (Liabilities transferred to Realisation A/c on dissolution)	Dr.	97,000	97,000
1.4.2022	*A*'s Loan A/c To Realisation A/c (Unrecorded asset of ₹25,000 accepted by *A* in full settlement of his loan)	Dr.	20,000	20,000
1.4.2022	Cash A/c To Realisation A/c (Furniture taken over by *B* for cash)	Dr.	1,66,250	1,66,250
1.4.2022	Cash A/c To Realisation A/c (Debtors collected through debt collection agency at a cost of ₹5,000)	Dr.	75,000	75,000
1.4.2022	Cash A/c To Realisation A/c (Stock realised)	Dr.	70,500	70,500
1.4.2022	Realisation A/c To *B*'s Capital A/c (Amount allowed to *B* for bearing all realisation expenses)	Dr.	500	500
1.4.2022	*A*'s Capital A/c *B*'s Capital A/c To Realisation A/c (Loss on realisation transferred to partners' capital accounts in their profit sharing ratio of 3 : 2) (Note 2)	Dr. Dr.	85,050 56,700	1,41,750
1.4.2022	*A*'s Capital A/c *B*'s Capital A/c To Cash A/c (Final payment made to partners on dissolution) (Note 3)	Dr. Dr.	2,14,950 1,43,800	3,58,750

Working Notes :

1. No entry is to be passed for building taken over by the creditors.
2. Calculation of Profit/Loss on realisation :

Dr. REALISATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Building	2,40,000	By Sundry Creditors	97,000
To Furniture	1,75,000	*A*'s Loan	20,000
To Debtors	80,000	By Cash (Furniture)	1,66,250
To Stock	75,000	By Cash (Debtors)	75,000
To *B*'s Capital A/c		By Cash (Stock)	70,500
(Realisation Expenses)	500	By Loss on Realisation	
		transferred to :	

		A's Capital A/c	85,050	
		B's Capital A/c	56,700	1,41,750
	5,70,500			5,70,500

3. Calculation of final payment made to the partners on dissolution :

PARTNERS' CAPITAL ACCOUNTS

Dr. Cr.

Particulars	*A*	*B*	*Particulars*	*A*	*B*
	₹	₹		₹	₹
To Realisation A/c (Loss)	85,050	56,700	By Balance b/d	3,00,000	2,00,000
To Cash (Final settlement)	2,14,950	1,43,800	By Realisation A/c (Realisation Exp.)	—	500
	3,00,000	2,00,500		3,00,000	2,00,500

Balance Sheet at the Date of Dissolution not Given

ILLUSTRATION 14.

Brahma, Vishnu and Mahesh are in partnership sharing in 3 : 3 : 4. They decided to dissolve the partnership firm. At the date of dissolution their creditors amounted to ₹16,000 and in the course of dissolution a contingent liability of ₹2,650 not brought into the accounts matured and had to be met. Their capitals stood at ₹12,000; ₹10,000 and ₹8,000 respectively. Vishnu had lent to the firm, in addition to capital ₹14,000. The assets realised ₹40,150.

Prepare the realisation account and the partner's capital accounts. Also show the cash account.

SOLUTION :

If a balance sheet on the date of dissolution is not given in the question, first of all, the Balance Sheet in proper form should be prepared in order to find out the missing figure :—

BALANCE SHEET

Liabilities		₹	*Assets*	₹
Creditors		16,000	Sundry Assets (Balancing figure)	60,000
Vishnu's Loan		14,000		
Capital Accounts :				
Brahma	12,000			
Vishnu	10,000			
Mahesh	8,000	30,000		60,000
		60,000		

REALISATION ACCOUNT

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Sundry Assets	60,000	By Creditors A/c	16,000

To Cash Account :			By Cash A/c		40,150
Creditors	16,000		By Loss on Realisation :		
Contingent Liability	2,650	18,650	Brahma's Capital A/c	6,750	
			Vishnu's Capital A/c	6,750	
			Mahesh's Capital A/c	9,000	22,500
		78,650			78,650

Dr. VISHNU'S LOAN ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Cash A/c	14,000	By Bal. b/d	14,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	Brahma	Vishnu	Mahesh	Particulars	Brahma	Vishnu	Mahesh
	₹	₹	₹		₹	₹	₹
To Realisation A/c (Loss)	6,750	6,750	9,000	By Balance b/d	12,000	10,000	8,000
To Cash A/c (Final Payment)	5,250	3,250	—	By Cash A/c (Amount brought in)	—	—	1,000
	12,000	10,000	9,000		12,000	10,000	9,000

Dr. CASH ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Realisation A/c (Assets realised)	40,150	By Realisation A/c (Liabilities paid)	18,650
To Mahesh's Capital A/c	1,000	By Vishnu's Loan A/c	14,000
		By Brahma's Capital A/c	5,250
		By Vishnu's Capital A/c	3,250
	41,150		41,150

ILLUSTRATION 15.

A and *B*, who were sharing profits and losses in the ratio of 60% and 40% respectively, decided to dissolve the firm on 31st March, 2022 on which date some of the balances were as follows :

	₹
A's Capital	2,40,000
B's Capital (Debit Balance)	25,000
Profit & Loss A/c (Debit Balance)	30,000
Trade Creditors	40,000
Loan from Mrs. *A*	20,000
Cash at Bank	15,000

The assets (other than cash at bank) realised ₹1,90,000 and **all creditors** were paid off less 5% discount. Realisation expenses amounted to ₹4,000.

Prepare Realisation Account, Capital Accounts and Bank Account assuming that both the partners are solvent.

SOLUTION:

BALANCE SHEET
as at 31st March, 2022

Liabilities	₹	*Assets*	₹
Trade Creditors	40,000	Cash at Bank	15,000
Loan from Mrs. *A*	20,000	*B*'s Capital	25,000
A's Capital	2,40,000	Profit & Loss A/c	30,000
		Sundry Assets (Balancing figure)	2,30,000
	3,00,000		3,00,000

Dr. REALISATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Sundry Assets A/c	2,30,000	By Trade Creditors		40,000
To Bank A/c (Trade Creditors paid off : ₹40,000 *less* 5%)	38,000	By Loan from Mrs. A		20,000
To Bank A/c (Loan from Mrs. *A* paid off : ₹20,000 *less* 5%)	19,000	By Bank A/c (Assets Realised)		1,90,000
To Bank A/c (Expenses of Realisation)	4,000	By Loss on Realisation :		
		A's Capital A/c 60%	24,600	
		B's Capital A/c 40%	16,400	41,000
	2,91,000			2,91,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*Particulars*	*A*	*B*
	₹	₹		₹	₹
To Balance b/d		25,000	By Balance b/d	2,40,000	
To Profit & Loss A/c	18,000	12,000	By Bank A/c (Amount brought in)		53,400
To Realisation A/c (Loss)	24,600	16,400			
To Bank A/c (Final Payment)	1,97,400				
	2,40,000	53,400		2,40,000	53,400

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	15,000	By Realisation A/c (Trade Creditors paid off)	38,000
To Realisation A/c (Assets realised)	1,90,000	By Realisation A/c (Loan from Mrs. *A* paid off)	19,000
To *B*'s Capital A/c	53,400	By Realisation A/c (Expenses)	4,000
		By *A*'s Capital A/c	1,97,400
	2,58,400		2,58,400

ILLUSTRATION 16.

A and *B* were partners in a business sharing profits and losses in the ratio of 3 : 1. They decided to dissolve the partnership on March 31, 2022. On that date, their Capitals stood at ₹1,00,000 and ₹50,000 respectively. Amount owing by *A* to the firm

was ₹42,000 and the amount owed by the firm to *B* was ₹15,000; Creditors were ₹25,000 and Cash ₹5,000. The assets other than the amount owing by *A* to the firm realised ₹64,000. The expenses of realisation amounted to ₹1,000.

Prepare the Memorandum Balance Sheet of the firm immediately prior to dissolution and necessary ledger accounts to close the books of the firm.

SOLUTION :

MEMORANDUM BALANCE SHEET
as at March 31, 2022

Liabilities		₹	*Assets*	₹
Creditors		25,000	Cash	5,000
B's Loan		15,000	*A*'s Loan	42,000
Capitals :			Other Assets (Balancing figure)	1,43,000
A	1,00,000			
B	50,000	1,50,000		
		1,90,000		1,90,000

Dr. REALISATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Sundry Assets	1,43,000	By Creditors		25,000
To Cash A/c (Creditors paid)	25,000	By Cash A/c (Assets realised)		64,000
To Cash A/c (Expenses)	1,000	By Loss transferred to :		
		A's Capital A/c 3/4th	60,000	
		B's Capital A/c 1/4th	20,000	80,000
	1,69,000			1,69,000

Dr. *B*'s LOAN ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Cash A/c	15,000	By Balance b/d	15,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*Particulars*	*A*	*B*
	₹	₹		₹	₹
To *A*'s Loan A/c	42,000		By Balance b/d	1,00,000	50,000
To Realisation A/c (Loss)	60,000	20,000	By Cash A/c	2,000	
To Cash A/c		30,000			
	1,02,000	50,000		1,02,000	50,000

Dr. CASH ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	5,000	By Realisation A/c (Creditors)	25,000
To Realisation A/c (Assets realised)	64,000	By Realisation A/c (Expenses)	1,000
To *A*'s Capital A/c	2,000	By *B*'s Loan A/c	15,000
		By *B*'s Capital A/c	30,000
	71,000		71,000

ILLUSTRATION 17.

On 1st April, 2021, *X*, *Y* and *Z* started business sharing profit and losses in the ratio of 3 : 2 : 1 respectively. They contributed ₹1,00,000, ₹80,000 and ₹40,000 respectively as their Capital which was deposited into Bank. Each Partner withdrew ₹15,000 during the year. The firm was dissolved on 31st March, 2022. *X* took up the stock at an agreed price of ₹25,000. *Y* took up furniture at ₹5,000 and *Z* took up debtors at ₹18,500. Creditors were paid off and then remained a balance of ₹14,000 in the Bank Account.

Prepare the necessary accounts to show the distribution of cash at bank and of the further cash brought in by any of the Partners.

SOLUTION :

BALANCE SHEET
as at 31st March, 2022

Liabilities		₹	*Assets*	₹
X's Capital :			Sundry Assets	
Opening	1,00,000		(Balancing figure)	1,75,000
Less : Drawings	15,000	85,000		
Y's Capital :				
Opening	80,000			
Less : Drawings	15,000	65,000		
Z's Capital :				
Opening	40,000			
Less : Drawings	15,000	25,000		
		1,75,000		1,75,000

Dr. REALISATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Sundry Assets	1,75,000	By *X*'s Capital A/c (Stock)		25,000
		By *Y*'s Capital A/c (Furniture)		5,000
		By *Z*'s Capital A/c (Debtors)		18,500
		By Bank A/c(1)		14,000
		By Loss transferred to :		
		X's Capital A/c	56,250	
		Y's Capital A/c	37,500	
		Z's Capital A/c	18,750	1,12,500
	1,75,000			1,75,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*X* ₹	*Y* ₹	*Z* ₹	*Particulars*	*X* ₹	*Y* ₹	*Z* ₹
To Realisation A/c (Assets taken)	25,000	5,000	18,500	By Balance b/d	85,000	65,000	25,000
To Realisation A/c (Loss)	56,250	37,500	18,750	By Bank (Deficit brought in)	—	—	12,250

To Bank A/c	3,750	22,500	—				
	85,000	65,000	37,250		85,000	65,000	37,250

Dr. BANK ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Realisation A/c		By *X*'s Capital A/c	3,750
(Net Assets realised)	14,000	By *Y*'s Capital A/c	22,500
To *Z*'s Capital A/c	12,250		
	26,250		26,250

Note : (1) Creditors must have been paid off out of the cash realised on sale of assets. Hence, ₹14,000 is the net amount realised on the sale of assets. Entry will be :

Bank A/c	Dr.	14,000	
To Realisation A/c			14,000

ILLUSTRATION 18.

L, *M* and *N* entered into Partnership on 1st April, 2021 sharing profits in the ratio of 4 : 3 : 3. Their Capitals were ₹60,000; ₹40,000 and ₹30,000 respectively. They decided to dissolve on 31st March, 2022, on which date their position was :

Bank ₹7,000; Debtors ₹40,000; B/R ₹5,500; Stock ₹43,000; Furniture ₹2,500; Creditors ₹15,000 and B/P ₹5,000.

L took over Debtors at 25% discount and took over the liabilities of the payment to creditors. *M* took over stock at ₹13,000. *N* takes B/R at ₹5,000 and furniture at 12% depreciation. B/P were due after 2 months; As such, a rebate of 18% p.a. was received on their payment.

10% p.a. interest is to be credited to each partner on his capital. Prepare necessary accounts.

SOLUTION :

If a Balance Sheet in proper form is not given in the question, first of all, a Balance Sheet should be prepared to find out any missing figure therein :

BALANCE SHEET
as at 31st March, 2022

Liabilities		₹	Assets	₹
Sundry Creditors		15,000	Bank Balance	7,000
Bills Payable		5,000	Debtors	40,000
Capitals :			Bills Receivable	5,500
L	60,000		Stock	43,000
M	40,000		Furniture	2,500
N	30,000	1,30,000	Profit & Loss (Balancing figure is assumed as loss)	52,000
		1,50,000		1,50,000

Note : Interest on Capital is allowed only in case of profits. In this question, there is loss of ₹52,000, as such, interest on Capital will not be allowed.

REALISATION A/C

Dr. Particulars	₹	Particulars		Cr. ₹
To Debtors	40,000	By Sundry Creditors		15,000
To Bills Receivable	5,500	By Bills Payable		5,000
To Stock	43,000	By L's Capital A/c (Debtors)		30,000
To Furniture	2,500	By M's Capital A/c (Stock)		13,000
To L's Capital A/c (Creditors)	15,000	By N's Capital A/c		7,200
To Bank A/c (B/P paid)	4,850	(B/R and Furniture)		
		By Loss transferred to :		
		L's Capital A/c	16,260	
		M's Capital A/c	12,195	
		N's Capital A/c	12,195	40,650
	1,10,850			1,10,850

CAPITAL ACCOUNTS

Dr. Particulars	L ₹	M ₹	N ₹	Particulars	L ₹	M ₹	Cr. N ₹
To P & L A/c	20,800	15,600	15,600	By Bal. b/d	60,000	40,000	30,000
To Realisation				By Realisation			
(Assets Taken)	30,000	13,000	7,200	(Creditors)	15,000		
To Realisation				By Bank A/c		795	4,995
(Loss)	16,260	12,195	12,195				
To Bank A/c	7,940						
	75,000	40,795	34,995		75,000	40,795	34,995

BANK ACCOUNT

Dr. Particulars	₹	Particulars	Cr. ₹
To Bal. b/d	7,000	By Realisation (B/P)	4,850
To M's Capital A/c	795	By L's Capital A/c	7,940
To N's Capital A/c	4,995		
	12,790		12,790

ILLUSTRATION 19.

A, *B* and *C* started business on 1st April, 2021, sharing profits in the ratio of 3 : 2 : 1. Their combined capital was ₹96,000 which was shared in profit sharing ratio. They are entitled to 10% p.a. interest on capitals. Profits for the year ending 31st March, 2022, before allowing interest on capitals were ₹39,600. They drew ₹10,000; ₹7,500 and ₹6,000 respectively during the year.

They decided to dissolve the firm on 31st March, 2022. Their creditors as on that date were ₹50,000. In addition, *A* had given a loan of ₹5,000 to the firm. There were liabilities amounting to ₹12,000, not shown in the books. These are also to be paid.

Assets realised for ₹1,20,000. Creditors for ₹40,000 were taken over by *A* for ₹36,000. Balance of the creditors were paid at a discount of 5%.

Prepare necessary accounts.

SOLUTION : PROFIT & LOSS APPROPRIATION ACCOUNT

For the year ending 31st March, 2022

Dr. Cr.

Particulars		₹	*Particulars*	₹
To Interest on Capitals:			By Balance b/d	
A	4,800		(Profit for the year 2018)	39,600
B	3,200			
C	1,600	9,600		
To Profit transferred to :				
A's Capital A/c 3/6	15,000			
B's Capital A/c 2/6	10,000			
C's Capital A/c 1/6	5,000	30,000		
		39,600		39,600

BALANCE SHEET *as at 31st March, 2022*

Liabilities		₹	*Assets*	₹
Creditors		50,000	Sundry Assets	
A's Loan		5,000	(Balancing Figure)	1,67,100
A's Capital :	48,000			
Add: Int. on Capital	4,800			
Add: Net Profit	15,000			
	67,800			
Less: Drawings	10,000	57,800		
B's Capital :	32,000			
Add: Int. on Capital	3,200			
Add: Net Profit	10,000			
	45,200			
Less: Drawings	7,500	37,700		
C's Capital :	16,000			
Add: Int. on Capital	1,600			
Add: Net Profit	5,000			
	22,600			
Less: Drawings	6,000	16,600		
		1,67,100		1,67,100

REALISATION ACCOUNT

Dr. Cr.

Particulars	₹	*Particulars*		₹
To Sundry Assets	1,67,100	By Creditors		50,000
To Cash A/c (Liabilities paid)	12,000	By Cash A/c		1,20,000
To *A* (Creditors taken)	36,000	By Loss transferred to :		
To Cash A/c (Creditors paid)	9,500	*A*'s Capital A/c	27,300	
		B's Capital A/c	18,200	
		C's Capital A/c	9,100	54,600
	2,24,600			2,24,600

A's LOAN ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Cash A/c	5,000	By Bal. b/d	5,000

CAPITAL ACCOUNTS

Dr. Cr.

Particulars	A	B	C	Particulars	A	B	C
	₹	₹	₹		₹	₹	₹
To Realisation (Loss)	27,300	18,200	9,100	By Bal. b/d	57,800	37,700	16,600
To Cash A/c (Final payment)	66,500	19,500	7,500	By Realisation (Creditors)	36,000		
	93,800	37,700	16,600		93,800	37,700	16,600

CASH ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Realisation A/c	1,20,000	By Realisation A/c	12,000
		By Realisation (Creditors paid)	9,500
		By A's Loan	5,000
		By A's Capital A/c	66,500
		By B's Capital A/c	19,500
		By C's Capital A/c	7,500
	1,20,000		1,20,000

ILLUSTRATION 20.

A & *B* were partners in a firm from 1.4.2020 with capitals of ₹60,000 and ₹40,000 respectively. They shared profits and losses in the ratio of 3 : 2. They carried on business for 2 years. In the first year they made a profit of ₹50,000 and in the 2nd year ending 31st March 2022, they incurred a loss of ₹20,000. As the business was no longer profitable they decided to wind up. Creditors on that date were ₹20,000. The partners withdrew ₹8,000 each per year for their personal expenses. The assets realised ₹1,00,000. The expenses on realisation were ₹3,000. Prepare Realization Account and show your workings clearly.

SOLUTION :

In this question, the Balance Sheet of the firm on the date of dissolution is not given. For that, we will have to prepare partner's Capital Accounts for the years ending 31st March 2021 and 2022 to ascertain the balance of capitals as on 31st March 2022.

CAPITAL ACCOUNTS

Dr. Cr.

Date	Particulars	A	B	Date	Particulars	A	B
2021		₹	₹	2020		₹	₹
March 31	To Drawings A/c	8,000	8,000	April 1	By Bank A/c	60,000	40,000
March 31	To Balance c/d	82,000	52,000	2021 March 31	By Profit & Loss Appropriation		

					A/c	30,000	20,000
		90,000	60,000			90,000	60,000
2022				2021			
March 31	To Drawings A/c	8,000	8,000	April 1	By Balance b/d	82,000	52,000
March 31	To Profit & Loss A/c	12,000	8,000				
March 31	To Balance c/d	62,000	36,000				
		82,000	52,000			82,000	52,000

Following Balance Sheet will be prepared on 31st March, 2022 in order to find out the missing figure of Sundry Assets on the date of dissolution :

BALANCE SHEET

Liabilities		₹	*Assets*	₹
Creditors		20,000	Sundry Assets (Balancing Figure)	1,18,000
Capital A/cs : *A*	62,000			
B	36,000	98,000		
		1,18,000		1,18,000

Dr. REALISATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Sundry Assets A/c	1,18,000	By Creditors A/c		20,000
To Bank A/c (Creditors paid)	20,000	By Bank A/c (Assets realised)		1,00,000
To Bank A/c (Expenses on realisation)	3,000	By Loss on Realisation :		
		A's Capital A/c $\frac{3}{5}$	12,600	
		B's Capital A/c $\frac{2}{5}$	8,400	21,000
	1,41,000			1,41,000

ILLUSTRATION 21.

Prakash, Kiran and Rishab are partners in a firm sharing profit and losses in the ratio of 3 : 2 : 1. Their Balance Sheet as at 31st March 2006 stood as follows :

Liabilities		₹	*Assets*		₹
Creditors		25,000	Cash at Bank		2,000
Bills Payable		10,000	Debtors	20,000	
General Reserve		27,000	*Less* : Provision for Bad		
Workmen's Compensation Fund		3,000	Debts	2,000	18,000
Mrs. Prakash's Loan		5,000	Stock		25,200
Capitals :			Investments		20,000
Prakash	60,000		Bills Receivable		8,000
Kiran	40,000	1,00,000	Machinery		60,000
			Goodwill		6,000
			Profit & Loss A/c		19,800
			Rishab's Capital A/c		11,000
		1,70,000			1,70,000

On the above date the firm was dissolved and the following transactions took place:

(*i*) The assets were sold off for the following amounts : Stock ₹20,200; Debtors ₹15,000; Machinery ₹40,000; and Investments ₹18,000.

(*ii*) Kiran took over the bills receivable at ₹7,000 and the bills payable at book value.

(*iii*) There was an unrecorded asset of ₹4,000 which was sold for ₹1,200.

(*iv*) Prakash agreed to pay off his wife's loan.

(*v*) A contingent liability for a bill discounted at ₹8,000 was settled by Prakash.

(*vi*) Creditors were settled at a discount of 10% and goodwill realized ₹5,000.

(*vii*) Realization expenses were ₹2,100 which were met by Kiran.

You are required to :

(*a*) Pass the necessary Journal Entries.

(*b*) Prepare the Realisation Account on the dissolution of the firm.

(*c*) Prepare the Capital Accounts of the Partners. *(I.S.C. 2007)*

SOLUTION :

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	*Particulars*		₹
To Debtors		20,000	By Provision for Bad Debts		2,000
To Stock		25,200	By Creditors		25,000
To Investments		20,000	By Bills Payable		10,000
To Bills Receivable		8,000	By Mrs. Prakash Loan		5,000
To Machinery		60,000	By Bank (Assets realised) :		
To Goodwill		6,000	Stock	20,200	
To Kiran's Capital A/c :			Debtors	15,000	
Bills Payable	10,000		Machinery	40,000	
Realisation Expenses	2,100	12,100	Investments	18,000	93,200
To Prakash's Capital A/c			By Kiran's Capital A/c		
Wife's Loan	5,000		(Bills Receivable)		7,000
Contingent liability			By Bank (Unrecorded Asset)		1,200
for Bill Discounted	8,000	13,000	By Bank (Goodwill)		5,000
To Bank (Creditors)		22,500	By Loss transferred to :		
			Prakash's Capital A/c	19,200	
			Kiran's Capital A/c	12,800	
			Rishab's Capital A/c	6,400	38,400
		1,86,800			1,86,800

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*Prakash*	*Kiran*	*Rishab*	*Particulars*	*Prakash*	*Kiran*	*Rishab*
	₹	₹	₹		₹	₹	₹
To Bal. b/d			11,000	By Bal. b/d	60,000	40,000	
To Profit & Loss A/c	9,900	6,600	3,300	By General Reserve	13,500	9,000	4,500

To Realisation A/c (Bills Receivable)		7,000		By Workmen's Compensation Fund(1)	1,500	1,000	500
To Realisation A/c (Loss)	19,200	12,800	6,400	By Realisation A/c (B/P and Realisation exp.)		12,100	
To Bank A/c (Final Payment)	58,900	35,700		By Realisation A/c (Wife Loan & contingent liability)	13,000		
				By Bank A/c (Amount brought in)			15,700
	88,000	62,100	20,700		88,000	62,100	20,700

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	2,000	By Realisation A/c (Creditors)	22,500
To Realisation A/c (Assets Realised)	93,200	By Prakash's Capital A/c	58,900
To Realisation A/c (Unrecorded Assets)	1,200	By Kiran's Capital A/c	35,700
To Realisation A/c (Goodwill realised)	5,000		
To Rishab's Capital A/c	15,700		
	1,17,100		1,17,100

Note (1) No compensation is payable to workmen. Hence, the entire amount of Workmen Compensation Fund is distributed among the partners in their profit sharing ratio.

ISC Council's Instruction

Partner's Current Accounts balances are to be transferred to Capital Accounts. No adjustments are required to be passed through Current Accounts.

ILLUSTRATION 22.

A, *B* and *C* sharing profits equally, dissolved their firm on 30th June, 2018, at which date their Balance Sheet was as follows :

Liabilities	₹	*Assets*	₹
Sundry Creditors	31,000	Bank	6,300
Reserve for contingency	18,000	Debtors	55,000
Profit & Loss A/c	12,000	Stock	81,000
A's Wife Loan	12,000	Furniture	20,000
Bank Loan at 12%	20,000	Plant	53,700
Capital Accounts : *A*	60,000	Current Account : *C*	22,000

	B	50,000		
	C	20,000		
Current Accounts :	A	10,000		
	B	5,000		
		2,38,000		2,38,000

(1) There is a bill for ₹5,000 under discount. This bill was received from '*R*'. *R* proved insolvent and 60% were received from his estate.

(2) It was found that an investment not recorded in the books is worth ₹8,000. This is taken over by one of the creditors at this value.

(3) *A* agreed to accept furniture in full settlement of his wife's loan.

(4) Bank Loan was repaid alongwith interest for nine months.

(5) Assets realised as follows : Debtors ₹24,500; Stock ₹60,000; Plant ₹28,000.

Prepare necessary accounts.

SOLUTION :

REALISATION ACCOUNT

Dr. Cr.

Particulars	₹	*Particulars*		₹
To Debtors	55,000	By Sundry Creditors		31,000
To Stock	81,000	By *A*'s Wife Loan		12,000
To Furniture	20,000	By Bank Loan at 12%		20,000
To Plant	53,700	By Bank (Assets realised)		1,12,500
To Bank (payment for bill discounted)	5,000	By Bank (Recovery from B/R dishonoured)		3,000
To Bank (payment to Creditors ₹31,000 *Less* : ₹8,000)	23,000	By Loss transferred to : *A*'s Capital A/c	27,000	
To Bank (payment of Bank Loan)	21,800	*B*'s Capital A/c	27,000	
		C's Capital A/c	27,000	81,000
	2,59,500			2,59,500

CAPITAL ACCOUNTS

Dr. Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To Current A/c (Transfer)	—	—	22,000	By Bal. b/d	60,000	50,000	20,000
To Realisation A/c (Loss)	27,000	27,000	27,000	By Current A/cs (Transfer)	10,000	5,000	—
To Bank A/c (Final payment)	53,000	38,000		By Reserve for contingency	6,000	6,000	6,000
				By P & L A/c	4,000	4,000	4,000
				By Bank A/c (Deficit brought in)			19,000
	80,000	65,000	49,000		80,000	65,000	49,000

BANK ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
To Balance b/d	6,300	By Realisation A/c (Bill discounted)	5,000
To Realisation A/c (Assets realised)	1,12,500	By Realisation A/c (Creditors)	23,000
To Realisation A/c (Recovery from B/R dishonoured)	3,000	By Realisation A/c (Bank Loan)	21,800
To C's Capital A/c	19,000	By A's Capital A/c	53,000
		By B's Capital A/c	38,000
	1,40,800		1,40,800

Working Notes :

(1) The Firm has to pay ₹5,000 to the bank for the dishonour of the discounted bill, of which 60% *i.e.,* ₹3,000 has been received from *R*. Following entries will be passed for it :

(*i*) Bank A/c	Dr.	3,000	
To Realisation A/c			3,000
(*ii*) Realisation A/c	Dr.	5,000	
To Bank A/c			5,000

(2) No separate entry will be passed for the Investments of ₹8,000, as these are taken over by the Creditors. Creditors will be paid at the net figure of ₹31,000 – ₹8,000 = ₹23,000.

(3) Wife's Loan has not been paid in Cash. It has been settled by giving away furniture. Therefore, no entry will be passed for the discharge of Wife's Loan.

ILLUSTRATION 23.

Erica, Aditi and Tarini were partners in a firm sharing profits and losses in the ratio of 5 : 3 : 2. Due to difference of opinion, they decided to dissolve the partnership with effect from 1st April, 2017, on which date the firm's Balance Sheet was as follows :

Balance Sheet of Erica, Aditi and Tarini
as at 1st April, 2017

Liabilities		₹	Assets		₹
Employees' Provident Fund		8,000	Cash at Bank		20,000
Sundry Creditors		10,000	Debtors	22,000	
Investment Fluctuation Reserve		4,000	*Less* : Prov. for d/d	(2,000)	20,000
Current Accounts :			Stock		12,000
Erica	8,000		Plant and Machinery		30,000
Aditi	10,000	18,000	Land & Building		45,000
Capital Accounts :			Investments		35,000
Erica	60,000		Advertisement Suspense A/c		3,000
Aditi	40,000		Current Account :		
Tarini	30,000	1,30,000	Tarini		5,000
		1,70,000			1,70,000

The following additional information was given :

(a) Plant & Machinery costing ₹20,000 was taken over by Erica at ₹16,000 and the remaining machineries realised ₹9,000.
(b) Land & Building realised ₹42,000.
(c) Investments were taken over by Aditi at ₹28,000.
(d) Sundry debtors included a bad debt for ₹1,000 and the amount was realised from the good debtors subject to a cash discount of 10%.
(e) A creditor for ₹2,000 was untraceable and other creditors accepted payments allowing 10% discount.
(f) Erica was allowed to retain the whole of the stock as her remuneration for services rendered by her in the course of dissolution of the firm.

You are required to prepare :

(i) Realisation Account.
(ii) Partners' Capital Accounts.
(iii) Bank Account.

(ISC Specimen Question Paper 2018)

SOLUTION :

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	*Particulars*		₹
To Debtors		22,000	By Employee's Provident Fund		8,000
To Stock		12,000	By Sundry Creditors		10,000
To Plant & Machinery		30,000	By Investment Fluctuation Reserve		4,000
To Land & Building		45,000	By Provision for Doubtful Debts		2,000
To Investments		35,000	By Erica's Capital A/c (Plant & Machinery taken over)		16,000
To Bank A/c (Payments) :			By Aditi's Capital A/c (Investments taken over)		28,000
Sundry Creditors 90% of (10,000 – 2,000)	7,200		By Bank A/c (Assets realised) :		
Employee's Provident Fund	8,000	15,200	Machinery	9,000	
			Land & Building	42,000	
			Debtors 90% of (22,000 – 1,000)	18,900	69,900
			By Loss on Realisation transferred to :		
			Erica's Capital A/c	10,650	
			Aditi's Capital A/c	6,390	
			Tarini's Capital A/c	4,260	21,300
		1,59,200			1,59,200

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*Erica*	*Aditi*	*Tarini*	*Particulars*	*Erica*	*Aditi*	*Tarini*
	₹	₹	₹		₹	₹	₹
To Current A/c	—	—	5,000	By Bal. b/d	60,000	40,000	30,000
To Advertise-ment Sus-				By Current A/cs	8,000	10,000	—

pense	1,500	900	600				
To Realisation A/c (Plant & Machinery	16,000						
To Realisation A/c (Investment)		28,000					
To Realisation A/c (Loss)	10,650	6,390	4,260				
To Bank A/c (Final Payment)	39,850	14,710	20,140				
	68,000	50,000	30,000		68,000	50,000	30,000

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	20,000	By Realisation A/c	
To Realisation A/c		(Liabilities Paid)	15,200
(Assets realised)	69,900	By Erica's Capital A/c	39,850
		By Aditi's Capital A/c	14,710
		By Tarini's Capital A/c	20,140
	89,900		89,900

Note : There will be no entry for stock taken over by Erica for her remuneration.

ILLUSTRATION 24.

Ram, Shyam and Mohan shared profits in the ratio of 2 : 2 : 1. Following is their Balance Sheet at the date of dissolution :

Liabilities	₹	*Assets*	₹
Creditors	40,000	Cash at Bank	44,000
Bills Payable	2,600	Debtors	15,000
Provision for Depreciation	15,000	Stock	50,000
Ram's Loan	40,000	Plant	75,000
Capital Accounts :		Patents	20,000
Ram	1,35,000	100 Shares in *X* Co.	5,000
Shyam	30,000	300 Shares in *Y* Co.	18,000
Mohan	10,000	Goodwill	15,600
		Advertisement Suspense A/c	30,000
	2,72,600		2,72,600

1. Ram takes over Debtors at ₹10,000; Stock at a 20% less value; and Plant at ₹30,000.

2. One of the Creditors took some of the patents whose book value was ₹8,000, at a valuation of ₹4,800. Balance of the creditors were paid at a discount of ₹1,200.

3. There was an unrecorded asset of ₹15,000 (not mentioned in the Balance Sheet) which was taken over by Ram at ₹10,000 in part payment of his loan.

4. Shares in *X* Co. were agreed to be taken over by Shyam at ₹30 per share.

5. Shares in *Y* Co. were valued at ₹12,000. All partners divided these shares in their profit sharing ratio.

6. Balance of the Patents realised 70% of their book value.

Prepare necessary ledger accounts.

SOLUTION :

Dr. REALISATION ACCOUNT Cr.

Particulars	₹	Particulars		₹
To Debtors	15,000	By Creditors		40,000
To Stock	50,000	By Bills Payable		2,600
To Plant	75,000	By Provision for Depreciation		15,000
To Patents	20,000	By Ram's Capital A/c (10,000 + 40,000 + 30,000)		80,000
To 100 Shares in *X* Co.	5,000	By Ram's Loan A/c (Unrecorded asset)		10,000
To 300 Shares in *Y* Co.	18,000	By Shyam's Capital A/c (Shares)		3,000
To Goodwill	15,600	By Ram's Capital A/c (Shares)		4,800
To Bank (payment to Creditors)	34,000	By Shyam's Capital A/c (Shares)		4,800
To Bank (B/P paid)	2,600	By Mohan's Capital A/c (Shares)		2,400
		By Bank A/c (Patents)		8,400
		By Loss transferred to :		
		Ram's Capital A/c	25,680	
		Shyam's Capital A/c	25,680	
		Mohan's Capital A/c	12,840	64,200
	2,35,200			2,35,200

Dr. RAM'S LOAN ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Realisation A/c (Asset taken)	10,000	By Balance b/d	40,000
To Bank A/c	30,000		
	40,000		40,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	Ram	Shyam	Mohan	Particulars	Ram	Shyam	Mohan
	₹	₹	₹		₹	₹	₹
To Advertisement Suspense A/c	12,000	12,000	6,000	By Bal. b/d	1,35,000	30,000	10,000
To Realisation A/c	80,000			By Bank A/c		15,480	11,240
To Realisation A/c		3,000					

To Realisation A/c (Shares of Y Co.)	4,800	4,800	2,400				
To Realisation (Loss)	25,680	25,680	12,840				
To Bank A/c	12,520						
	1,35,000	45,480	21,240		1,35,000	45,480	21,240

Dr. BANK ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance b/d	44,000	By Realisation A/c (Creditors)	34,000
To Realisation A/c (Patents)	8,400	By Realisation A/c (B/P)	2,600
To Shyam's Capital A/c	15,480	By Ram's Loan A/c	30,000
To Mohan's Capital A/c	11,240	By Ram's Capital A/c	12,520
	79,120		79,120

Notes : (1) Net amount paid to Creditors : ₹40,000 (–) 4,800 (–) 1,200 = ₹34,000.

(2) Entry for Ram's Loan :

Ram's Loan A/c	Dr.	40,000	
To Realisation A/c			10,000
To Bank A/c			30,000

ILLUSTRATION 25.

Girija and Ganesh were partners in a firm sharing profits and losses in the ratio of 2 : 3. On 31st March, 2017 their Balance Sheet was as follows :

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Creditors		80,000	Cash at Bank		20,000
Bank Overdraft		50,000	Debtors	55,000	
Girija's Brother's Loan		77,000	*Less* : Provision for		
Ganesh's loan		28,000	Doubtful Debts	2,000	53,000
Investment Fluctuation Fund		15,000	Stock		78,000
Capitals :			Investments		89,000
Girija	1,50,000		Buildings		2,50,000
Ganesh	1,00,000	2,50,000	Profit and Loss A/c		10,000
		5,00,000			5,00,000

On the above date the firm was dissolved. The assets were realized and the liabilities were paid off as follows :

(*a*) Debtors of ₹6,000 were proved bad.

(*b*) Girija agreed to pay off her brother's Loan.

(*c*) One of the creditors for ₹10,000 was paid only ₹3,000 in full settlement of his account.

(*d*) Buildings were auctioned for ₹1,80,000 and the auctioneer's commission amounted to ₹8,000.

(e) Ganesh took over part of stock at ₹4,000 (being 20% less than the book value). Balance of the Stock was handed over to the remaining creditors in full settlement of their account.

(f) Investments realized ₹9,000 less.

(g) Realisation expenses amounted to ₹17,000 and were paid by Ganesh.

Prepare Realisation Account, Partners' Capital Accounts and Bank Account.

(C.B.S.E. 2018, Comptt.)

SOLUTION :

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	*Particulars*		₹
To Sundry Assets :			By Sundry Liabilities :		
Debtors	55,000		Provision for		
Stock	78,000		Doubtful Debts	2,000	
Investments	89,000		Creditors	80,000	
Buildings	2,50,000	4,72,000	Girija's Brother's		
To Girija's Capital A/c			Loan	77,000	1,59,000
(Brother's Loan)		77,000	By Investment Flucturation		
To Bank A/c :			Fund		15,000
(Creditors)		3,000	By Bank A/c		
To Ganesh's Capital A/c			Debtors	49,000	
(Realisation Exp.)		17,000	Buildings	1,72,000	
			Investments	80,000	3,01,000
			By Ganesh's Capital A/c (Stock)		4,000
			By Loss transferred to :		
			Girija's Capital A/c	36,000	
			Ganesh's Capital A/c	54,000	90,000
		5,69,000			5,69,000

Dr. PARTNER'S CAPITAL ACCOUNTS Cr.

Particulars	*Girija* ₹	*Ganesh* ₹	*Particulars*	*Girija* ₹	*Ganesh* ₹
To P & L A/c	4,000	6,000	By Balance b/d	1,50,000	1,00,000
To Realisation A/c			By Realisation A/c		
(Stock)		4,000	(Brother's Loan)	77,000	
To Realisation A/c			By Realisation A/c		
(Loss)	36,000	54,000	(Exp.)		17,000
To Bank A/c	1,87,000	53,000			
	2,27,000	1,17,000		2,27,000	1,17,000

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Balance b/d	20,000	By Balance b/d (Bank Overdraft)	50,000
To Realisation A/c (Assets)	3,01,000	By Realisation A/c (Creditors)	3,000
		By Ganesh's Loan A/c	28,000

		By Girija's Capital A/c	1,87,000
		By Ganesh's Capital A/c	53,000
	3,21,000		3,21,000

ILLUSTRATION 26.

A, *B* and *C* shared profits in the ratio of 3 : 2 : 1. They dissolved the firm and appointed *A* to realise the assets. *A* is to receive 5% commission on the sale of assets (except cash) and is to bear all expenses of realisation. The position of the firm was as follows :

Liabilities	₹	*Assets*	₹
Bank overdraft	25,000	Cash in Hand	22,500
Creditors	60,000	Debtors	52,300
Provident Fund	12,000	Stock	36,000
Investment Fluctuation Fund	6,000	Investments	15,000
Commission Received in Advance	8,000	Plant	91,200
Capitals :		Profit & Loss A/c	54,000
A	90,000		
B	60,000		
C	10,000		
	2,71,000		2,71,000

Informations : 1. *A* realised the assets as follows:— Debtors ₹30,000; Stock ₹26,000; Investments at 75% value; Plant at ₹42,750. Expenses of realisation met by *A* amounted to ₹4,100.

2. Commission received in advance is returned to the customers after deducting ₹3,000 for work done.

3. Firm had to pay ₹7,200 for outstanding salaries, not provided for earlier.

4. Compensation to employees paid by the firm amounted to ₹9,800. This liability was not provided for in the above balance sheet.

5. ₹25,000 had to be paid for Provident Fund.

Prepare necessary accounts.

SOLUTION :

Dr. REALISATION ACCOUNT Cr.

Particulars	₹	*Particulars*		₹
To Debtors	52,300	By Creditors		60,000
To Stock	36,000	By Provident Fund		12,000
To Investments	15,000	By Investment Fluctuation Fund		6,000
To Plant	91,200	By Commission Recd. in advance		8,000
To *A*'s Capital A/c		By Bank A/c :		
(5% on ₹1,10,000)	5,500	Debtors	30,000	
To Bank A/c (Advance	5,000	Stock	26,000	
Commission returned)		Investments	11,250	
To Bank A/c (Outstanding	7,200	Plant	42,750	1,10,000
salaries paid)		By Loss transferred to :		

To Bank A/c (Compensation paid)	9,800	*A*'s Capital A/c	55,500	
To Bank A/c (Creditors and Provident Fund)	85,000	*B*'s Capital A/c	37,000	
		C's Capital A/c	18,500	1,11,000
	3,07,000			3,07,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*C*	*Particulars*	*A*	*B*	*C*
	₹	₹	₹		₹	₹	₹
To P & L A/c	27,000	18,000	9,000	By Bal. b/d	90,000	60,000	10,000
To Realisation (Loss)	55,500	37,000	18,500	By Realisation A/c (commission)	5,500		
To Bank A/c	13,000	5,000		By Bank A/c			17,500
	95,500	60,000	27,500		95,500	60,000	27,500

Dr. BANK ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Cash A/c (deposited)	22,500	By Balance b/d	25,000
To Realisation A/c (Assets realised)	1,10,000	By Realisation (Comm. returned)	5,000
To C's Capital A/c	17,500	By Realisation (Outstanding salary)	7,200
		By Realisation (Compensation)	9,800
		By Realisation (Creditors and Provident Fund)	85,000
		By *A*'s Capital A/c	13,000
		By *B*'s Capital A/c	5,000
	1,50,000		1,50,000

Notes : 1. There will be no entry for the expenses of realisation, as these are met by *A* personally.

2. Following entry will be passed for Commission payable to *A* on the sale of assets :

Realisation A/c	Dr.	5,500	
To *A*'s Capital A/c			5,500

ILLUSTRATION 27.

Field, Meadow and Park were in partnership sharing profit and losses equally. Their Balance Sheet as at 30th June, 2004 was as under :

Liabilities		₹	*Assets*	₹
Capital Accounts :			Plant and Machinery	19,010
Field	24,000		Furniture & Fixtures	3,392
Meadow	18,000		Sundry Debtors	11,330
Park	13,000	55,000	Patents	9,684
Sundry Creditors		14,176	Bills Receivable	6,890
Bills Payable		6,720	Stock in Trade	23,950
Current Accounts :			Cash at Bank	3,360
Field	6,880		Current Account :	

Park	2,760	9,640	Meadow	7,920
		85,536		85,536

Field died on 1st July, 2004. The remaining partners could not arrive at any understanding with legal representatives of field. Consequently, it was decided that the firm would be dissolved, subject to the following adjustments :

(a) An unrecorded asset was realized for ₹24,000.

(b) Plant and Machinery realised only 70% of the book value.

(c) Furniture and Fixtures were taken over by partner Park at a market value of ₹2,000.

(d) Bills receivable and sundry debtors had to be discounted at 5%.

(e) Stock in trade comprised :

(i) Easily marketable items — 70% of the total inventory which were realized in full;

(ii) Obsolete items — 10% of the total inventory which had to be discarded;

(iii) The rest of the items in the stock realized 50% of their book value.

(f) A liability for ₹1,100 which had not been recorded in the books of the firm had to be settled by the firm before its dissolution.

You are required to prepare necessary accounts. (I.S.C. 2005)

SOLUTION:

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	*Particulars*		₹
To Sundry Assets :			By Sundry Liabilities :		
Plant and Machinery	19,010		Sundry Creditors	14,176	
Furniture & Fixtures	3,392		Bills Payable	6,720	20,896
Sundry Debtors	11,330		By Bank A/c :		
Patents	9,684		(Assets Realised)		
Bills Receivable	6,890		Unrecorded Asset	24,000	
Stock in Trade	23,950	74,256	Plant and Machinery	13,307	
To Bank A/c (payment of liability)		1,100	Bills Receivable	6,546	
To Bank A/c (payment of			Sundry Debtors	10,763	
Creditors and Bills Payable			Stock[1]	19,160	73,776
14,176 + 6,720)		20,896	By Park's Capital A/c		
To Profit on Realisation :			(Furniture & Fixtures taken		
Field's Capital A/c	140		over by Park)		2,000
Meadow's Capital A/c	140				
Park's Capital A/c	140	420			
		96,672			96,672

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*Field*	*Meadow*	*Park*	*Particulars*	*Field*	*Meadow*	*Park*
	₹	₹	₹		₹	₹	₹
To Current A/c				By Bal. b/d	24,000	18,000	13,000

(transfer)		7,920		By Current A/cs (transfer)	6,880		2,760
To Realisation A/c (Asset taken)			2,000	By Realisation (Profit)	140	140	140
To Bank A/c	31,020	10,220	13,900				
	31,020	18,140	15,900		31,020	18,140	15,900

Dr. BANK ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Bal. b/d	3,360	By Realisation A/c (Payment of liability)	1,100
To Realisation A/c (Assets Realised)	73,776	By Realisation A/c (Payment of Creditors and Bills Payable)	20,896
		By Field's Capital A/c	31,020
		By Meadow's Capital A/c	10,220
		By Park's Capital A/c	13,900
	77,136		77,136

Working Note : (1) Calculation of Stock Realised :

	₹
70% of 23,950 realised in full	= 16,765
10% of 23,950 realised nil	= —
20% of 23,950 realised 50%	= 2,395
	19,160

ILLUSTRATION 28.

A, *B* and *C* are partners in a firm sharing profits and losses in the ratio of $\frac{1}{2}:\frac{1}{3}:\frac{1}{6}$. At 31st March, 2019 their Balance Sheet was as follows :

Liabilities		₹	*Assets*		₹
Sundry Creditors		24,500	Plant		50,000
Mrs. *C*'s Loan		20,000	Freehold Property		1,12,000
Workmen Compensation Reserve		12,000	Patents		6,000
Capital Accounts :			Stock		40,000
A	1,00,000		Sundry Debtors	40,000	
B	80,000		*Less* : Provision	1,500	38,500
C	40,000	2,20,000	Prepaid Expenses		2,000
			Cash at Bank		28,000
		2,76,500			2,76,500

It was decided to dissolve the firm, *A* agreeing to take over the business (except cash at bank) at the following Valuations :

Plant at a depreciation of 20%; Freehold Property at ₹1,50,000; Goodwill at ₹10,000; Patents at book value; Sundry Debtors at ₹35,000 (Net); Half the Stock at 30% more than its book value and the remaining half at 50% *less* than the book value.

Mrs. C's loan was to be repaid and the Creditors were proved at ₹22,000 and were taken over by A. Expenses of dissolution came to ₹1,000.

Close the books of the firm and prepare the Balance Sheet of A.

SOLUTION :

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	Particulars		₹
To Plant		50,000	By Provision for Doubtful Debts		1,500
To Freehold Property		1,12,000	By Sundry Creditors		24,500
To Patents		6,000	By Mrs. C's Loan		20,000
To Stock		40,000	By A's Capital A/c :		
To Sundry Debtors		40,000	Plant	40,000	
To Bank (Mrs. C's Loan)		20,000	Freehold Property	1,50,000	
To Bank (Expenses)		1,000	Goodwill	10,000	
To Prepaid Expenses		2,000	Patents	6,000	
To Profit on Realisation :			Sundry Debtors	35,000	
A's Capital A/c 1/2	15,000		Stock	36,000	
B's Capital A/c 1/3	10,000			2,77,000	
C's Capital A/c 1/6	5,000	30,000	*Less :* Creditors	22,000	2,55,000
		3,01,000			3,01,000

Dr. CAPITAL ACCOUNTS Cr.

Particulars	A ₹	B ₹	C ₹	Particulars	A ₹	B ₹	C ₹
To Realisation	2,55,000			By Balance b/d	1,00,000	80,000	40,000
To Bank		94,000	47,000	By Workmen Compensation Reserve	6,000	4,000	2,000
				By Realisation (Profit)	15,000	10,000	5,000
				By Bank	1,34,000		
	2,55,000	94,000	47,000		2,55,000	94,000	47,000

Dr. BANK ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance b/d	28,000	By Mrs. C's Loan	20,000
To A's Capital A/c	1,34,000	By Realisation (Expenses)	1,000
		By B's Capital A/c	94,000
		By C's Capital A/c	47,000
	1,62,000		1,62,000

BALANCE SHEET OF A *as at 31st March, 2019*

Liabilities	₹	*Assets*	₹
Sundry Creditors	22,000	Goodwill	10,000

Capital	2,55,000	Freehold Property		1,50,000
		Plant		40,000
		Patents		6,000
		Stock		36,000
		Sundry Debtors	40,000	
		Less : Provision	5,000	35,000
	2,77,000			2,77,000

ILLUSTRATION 29.

Give the necessary journal entries in each of the following alternative cases :

(*i*) Realization expenses amounted to ₹500.

(*ii*) Realization expenses paid by the firm amounted to ₹500 and the partner has to bear the realization expenses.

(*iii*) '*A*' one of the partners was to bear all the realisation expenses for which he was given a commission of 2% of net cash realised from dissolution. Cash realised from assets was ₹25,000 and cash paid for liabilities amounted to ₹5,000.

SOLUTION:

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
(*i*)	Realisation A/c	Dr.		500	
	To Bank A/c				500
	(Payment of realisation expenses)				
(*ii*)	Partner's Capital A/c	Dr.		500	
	To Bank A/c				500
	(Payment of realisation expenses by the firm on behalf of the partner)				
(*iii*)	Bank A/c	Dr.		25,000	
	To Realisation A/c				25,000
	(Amount realised on sale of assets)				
	Realisation A/c	Dr.		5,000	
	To Bank A/c				5,000
	(Amount paid for liabilities)				
	Realisation A/c	Dr.		400	
	To *A*'s Capital A/c				400
	(Commission allowed to *A* @ 2% on ₹20,000 *i.e.*, 25,000 – 5,000)				

ILLUSTRATION 30.

J, *K* and *L* were partners in a firm sharing profits in the ratio of 4 : 5 : 1. On 31st March, 2018 their firm was dissolved. On this date the Balance Sheet showed a balance of ₹1,34,000 in debtors account and a balance of ₹14,000 in provision for bad debts account. Both the accounts were closed by transferring their balances to realisation account. ₹4,000 of the debtors became bad and nothing could be realised

from them on dissolution. *K* agreed to look after the dissolution work for which he was allowed a remuneration of ₹16,000. *K* also agreed to bear dissolution expenses for which he was allowed a lumpsum payment of ₹4,000. Actual dissolution expenses were ₹6,500 and the same were paid from the firm's cash. Loss on dissolution amounted to ₹37,000.

Pass necessary journal entries for the above transactions in the books of the firm on its dissolution. *(C.B.S.E. 2019, Kerala)*

SOLUTION :

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2018 March 31					
(*a*)	Bank A/c	Dr.		1,30,000	
	To Realisation A/c				1,30,000
	(Amount realised from debtors)				
(*b*)	Realisation A/c	Dr.		20,000	
	To *K*'s Capital A/c				20,000
	(Remuneration for dissolution work and for dissolution expenses)				
(*c*)	*K*'s Capital A/c	Dr.		6,500	
	To Bank A/c				6,500
	(Dissolution expenses borne by *K* paid by firm)				
(*d*)	*J*'s Capital A/c	Dr.		14,800	
	K's Capital A/c	Dr.		18,500	
	L's Capital A/c	Dr.		3,700	
	To Realisation A/c				37,000
	(Realisation loss transferred to Partners' Capital A/cs)				

ILLUSTRATION 31 :

Ankit, Bobby and Kartik were partners in a firm sharing profits in the ratio 4 : 3 : 3. The firm was dissolved on 31-3-2018. Pass the necessary Journal entries for the following transactions after various assets (other than cash and bank) and third party liabilities had been transferred to Realisation Account :

(*i*) The firm had stock of ₹80,000. Ankit took over 50% of the stock at a discount of 20% while the remaining stock was sold off at a profit of 30% on cost.

(*ii*) A liability under a suit for damages included in creditors was settled at ₹32,000 as against only ₹13,000 provided in the books. Total creditors of the firm were ₹50,000.

(*iii*) Bobby's sister's loan of ₹20,000 was paid off along with interest of ₹2,000.

(*iv*) Kartik's Loan of ₹12,000 was settled at ₹12,500. *(C.B.S.E. 2019, M.P.)*

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2018 March, 31 (*i*)	Ankit's Capital A/c	Dr.		32,000	
	Bank A/c	Dr.		52,000	
	To Realisation A/c				84,000
	(Stock taken over by Ankit, remaining sold at a profit)				
(*ii*)	Realisation A/c	Dr.		69,000	
	To Bank A/c				69,000
	(Payment made to creditors ₹32,000 + ₹37,000)				
(*iii*)	Realisation A/c	Dr.		22,000	
	To Bank A/c				22,000
	(Bobby's sister's loan paid along with interest)				
(*iv*)	Kartik's loan A/c	Dr.		12,000	
	Realisation A/c	Dr.		500	
	To Bank A/c				12,500
	(Kartik's loan settled)				

ILLUSTRATION 32.

Ravi, Shankar and Madhur were partners in a firm sharing profits in the ratio of 7 : 2 : 1. On 31st March, 2018, the firm was dissolved, after transferring sundry assets (other than cash in hand and cash at bank) and third party liabilities in the realization account the following transactions took place :

(*i*) Debtors amounting to ₹1,40,000 were handed over to a debt collection agency which charged 5% commission. The remaining debtors were ₹47,000, out of which debtors of ₹17,000 could not be recovered because the same became insolvent.

(*ii*) Creditors amounting to ₹5,000 were paid ₹3,500 in full settlement of their claim and balance creditors were handed over stock of ₹90,000 in full settlement of their claim of ₹95,000.

(*iii*) A bills receivable ₹2,000 discounted with the bank was dishonoured by its acceptor and the same had to be met by the firm.

(*iv*) Profit on realisation amounted to ₹6,000.

Pass necessary journal entries for the above transactions in the books of Ravi, Shankar and Madhur. *(C.B.S.E. 2019, M.P.)*

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2018 March, 31 (*i*)	Bank A/c	Dr.		1,63,000	
	To Realisation A/c				1,63,000
	(Amount received from debtors)				

(ii)	Realisation A/c Dr. To Bank A/c (Payment made to creditors)			3,500	3,500
(iii)	Realisation A/c Dr. To Bank A/c (Discounted bill dishonoured)			2,000	2,000
(iv)	Realisation A/c Dr. To Ravi's Capital A/c To Shankar's Capital A/c To Madhur's Capital A/c (Profit on Realisation transferred to partners capital accounts)			6,000	4,200 1,200 600

ILLUSTRATION 33.

Give the necessary journal entries for the following transactions on dissolution of the firm of Anita and Ravi on 31st March 2016, after the various assets (other than cash) and the third party liabilities have been transferred to Realisation Account. They shared profits and losses in the ratio 3 : 2.

(*a*) Ravi was to get a remuneration of ₹23,000 for completing the dissolution process. He also agreed to bear realization expenses. Realisation expenses of ₹10,000 were paid by Ravi from the firm's cash.

(*b*) Amitesh, an old customer whose account for ₹60,000 was written off as bad debt in the previous year, paid 90%.

(*c*) Creditors of ₹40,000, accepted furniture valued at ₹38,000 in full settlement of their claim.

(*d*) Land and Building was sold for ₹3,00,000 through a broker who charged 2% commission.

(*e*) There were 500 shares of ₹40 each in Vision Ltd., acquired at a cost of ₹22,000 and had been written off completely from the books. These shares are now valued at ₹50 each and divided among the partners in their profit sharing ratio.

(*f*) Profit on realization was ₹45,000. *(C.B.S.E. 2017, Comptt. Outside Delhi)*

SOLUTION:

Books of Anita and Ravi

JOURNAL

Date	*Particulars*	*L.F.*	*Dr. Amount*	*Cr. Amount*
2016			₹	₹
March 31				
(*a*) (*i*)	Realisation A/c Dr. To Ravi's Capital A/c (Remuneration allowed to Ravi to carry out dissolution)		23,000	23,000
(*ii*)	Ravi's Capital A/c Dr. To Cash A/c (Realisation expenses paid by the firm and borne by Ravi)		10,000	10,000

(b)	Bank A/c Dr. To Realisation A/c (Amount recovered from debtor earlier written off as bad debts)		54,000	54,000
(c)	No entry			
(d)	Bank A/c Dr. To Realisation A/c (Amount realised from land and building after deducting commission)		2,94,000	2,94,000
(e)	Anita's Capital A/c Dr. Ravi's Capital A/c Dr. To Realisation A/c (500 Shares of ₹50 each transferred to Anita, Ravi in 3 : 2)		15,000 10,000	25,000
(f)	Realisation A/c Dr. To Anita's Capital A/c To Ravi's Capital A/c (Profit on realization transferred to Anita and Ravi in 3 : 2)		45,000	27,000 18,000

ILLUSTRATION 34.

Rohit, Kunal and Sarthak are partners in a firm. They decided to dissolve their firm. Pass necessary Journal entries for the following after various assets (other then Cash and Bank) and the third party liability have been transferred to Realisation Account :

(*a*) Kunal agreed to pay off his wife's loan of ₹6,000.

(*b*) Total Creditors of the firm were ₹40,000. Creditors worth ₹10,000 were given a piece of furniture costing ₹8,000 in full and final settlement. Remaining Creditors allowed a discount of 10%.

(*c*) Rohit had given a loan of ₹70,000 to the firm which was duly paid.

(*d*) A machine which was not recorded in the books was taken over by Kunal at ₹3,000, whereas its expected value was ₹5,000.

(*e*) The firm had a debit balance of ₹15,000 in the Profit and Loss Account on the date of dissolution.

(*f*) Sarthak paid the realisation expenses of ₹16,000 out of his private funds, who was to get a remuneration of ₹15,000 for completing dissolution process and was responsible to bear all the realisation expenses.

(C.B.S.E. Sample Paper, 2019)

SOLUTION : JOURNAL ENTRIES

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
(*a*)	Realisation A/c Dr. To Kunal's Capital A/c (Kunal agreed to pay off his wife loan)		6,000	6,000
(*b*)	Realisation A/c Dr. To Bank A/c (Payment made to Creditors) (Note 1)		27,000	27,000

(c)	Rohit's Loan A/c Dr. To Bank A/c (Rohit's loan paid off)		70,000	70,000
(d)	Kunal's Capital A/c Dr. To Realisation A/c (Unrecorded machine taken over by Kunal)		3,000	3,000
(e)	Rohit's Capital A/c Dr. Kunal's Capital A/c Dr. Sarthak's Capital A/c Dr. To Profit and Loss A/c (Accumulated losses distributed among the partners)		5,000 5,000 5,000	15,000
(f)	Realisation A/c Dr. To Sarthak's Capital A/c (Remuneration due to Sarthak)		15,000	15,000

			₹
Note (1) :	Total Creditors		40,000
	Less :	Settled against furniture	10,000
			30,000
	Less :	10% Discount	3,000
			27,000

ILLUSTRATION 35.

Parul, Payal and Priyanka are partners. They decided to dissolve their firm. Pass necessary journal entries for the following after various assets (other than cash and bank) and the third party liabilities have been transferred to Realisation Account :

(*a*) There were total debtors of ₹76,000. A provision of bad and doubtful debts also stood in the books at ₹6,000. ₹12,000 debtors proved bad and rest paid the amount due.

(*b*) Parul agreed to pay off her husband's loan of ₹7,000 at a discount of 5%.

(*c*) A machine which was not recorded in the books was taken over by Payal at ₹3,000, whereas its expected value was ₹5,000.

(*d*) A contingent liability (not provided for) of ₹4,000 was also discharged.

(*e*) The firm had a debit balance of ₹27,000 in the Profit and Loss Account on the date of dissolution.

(*f*) Priyanka paid the realisation expenses of ₹15,000 out of her pocket and she was to get a fixed remuneration of ₹18,000 for completing the dissolution process.

SOLUTION : JOURNAL

Date	*Particulars*	*L.F.*	*Dr.* (₹)	*Cr.* (₹)
(*a*)	Bank A/c (76,000 – 12,000) Dr. To Realisation A/c (Debtors realised)		64,000	64,000
(*b*)	Realisation A/c (7,000 – 350) Dr. To Parul's Capital A/c (Husband's loan taken over by Parul at a discount of 5%)		6,650	6,650

(c)	Payal's Capital A/c Dr. To Realisation A/c (Unrecorded machine taken over by Payal)		3,000	3,000
(d)	Realisation A/c Dr. To Bank A/c (Payment of contingent liability)		4,000	4,000
(e)	Parul's Capital A/c Dr. Payal's Capital A/c Dr. Priyanka's Capital A/c Dr. To Profit and Loss A/c (Transfer of debit balance of profit and loss account)		9,000 9,000 9,000	27,000
(f)	Realisation A/c Dr. To Priyanka's Capital A/c (Realisation expenses of ₹15,000 paid by Priyanka now reimbursed and remuneration allowed to Priyanka ₹18,000 also credited to her account.)		33,000	33,000

ILLUSTRATION 36.

P and *Q* were partners in a firm. Pass journal entries for the following transactions on dissolution of the firm after various assets and external liabilities have been transferred to Realisation A/c.

(*i*) *X*, an unrecorded creditor of ₹10,000 was paid by partner *P* at a discount of 20%.

(*ii*) *Y*, an unrecorded creditor of ₹25,000, took over Computer at ₹30,000. Balance was paid by him in Cash.

(*iii*) There was an unrecorded asset of ₹20,000 half of which was handed over to settle half of the unrecorded liability of ₹28,000 and the balance of the unrecorded liability was paid at 80% in full settlement. The remaining half of the unrecorded asset was sold in the market at a discount of 10%.

(*iv*) There was a Contingent liability in respect of bill discounted but not matured of ₹75,000. An acceptor of one bill of ₹25,000 became insolvent and sixty paise in a rupee were recovered. This liability for bill discounted has not been recorded so far.

(*v*) Computer of ₹25,000 and a Vehicle of ₹10,000 were appearing in the Balance Sheet but no other additional information was given regarding these items.

(*vi*) *P*'s loan was appearing on the liabilities side of the Balance Sheet at ₹50,000. He accepted an unrecorded asset of ₹40,000 at ₹35,000 and the balance was paid to him in Cash.

SOLUTION:

JOURNAL

Date	*Particulars*	*L.F.*	*Dr. (₹)*	*Cr. (₹)*
(*i*)	Realisation A/c Dr. To *P*'s Capital A/c (Unrecorded liability taken over by *P* at a discount of 20%)		8,000	8,000

(ii)	Bank A/c Dr. To Realisation A/c (Cash received from unrecorded creditor)		5,000	5,000
(iii)	Realisation A/c Dr. To Bank A/c (Half of unrecorded liability of ₹28,000 *i.e.*, ₹14,000 settled at 80%)		11,200	11,200
	Bank A/c Dr. To Realisation A/c (Half of unrecorded asset of ₹20,000 *i.e.*, ₹10,000 sold at 10% discount)		9,000	9,000
(iv)	Realisation A/c Dr. To Bank A/c (Payment made to bank for bill discounted and dishonoured)		25,000	25,000
	Bank A/c Dr. To Realisation A/c (60% of the dishonoured bill recovered)		15,000	15,000
(v)	No entry			
(vi)	P's Loan A/c Dr. To Realisation A/c To Bank A/c (*P*'s loan settled by giving unrecorded asset of ₹35,000 and the balance in Cash)		50,000	35,000 15,000

ILLUSTRATION 37.

Following is the Balance Sheet of Ravi and Prakash as at 31st March, 2012 :

Liabilities	₹	*Assets*		₹
Sundry Creditors	60,000	Cash		25,000
Ravi's Loan	15,000	Debtors	42,000	
General Reserve	15,000	*Less* : Provision for		
Investments Fluctuation Reserve	2,000	Doubtful Debts	(6,000)	36,000
Ravi's Capital	30,000	Stock		12,000
Prakash's Capital	10,000	Investments		18,000
		Plant and Machinery		41,000
	1,32,000			1,32,000

The firm was dissolved on 31st March, 2012, on the following terms :

(*a*) Ravi took over stock at ₹8,000.

(*b*) Creditors payable after two months were paid immediately at a discount of 6% p.a.

(*c*) Debtors realised ₹35,000.

(*d*) Plant and Machinery and Investments realised ₹60,000.

(*e*) An old computer completely written off was taken over by Prakash at ₹1,200.

(*f*) Realisation expenses of ₹2,000 were paid by Ravi.

You are required to prepare :

(i) Realisation Account.

(ii) Partners' Capital Accounts.

(iii) Cash Account.

(I.S.C. 2013)

SOLUTION :

REALISATION ACCOUNT

Dr. Cr.

Particulars	₹	Particulars		₹
To Debtors	42,000	By Provision for Doubtful Debts		6,000
To Stock	12,000	By Sundry Creditors		60,000
To Investments	18,000	By Investments Fluctuation Reserve		2,000
To Plant and Machinery	41,000	By Ravi's Capital A/c (Stock)		8,000
To Cash A/c (Creditors)	59,400	By Cash A/c (Assets) :		
To Ravi's Capital A/c (Realisation Expenses)	2,000	Debtors	35,000	
		Plant and Machinery and Investments	60,000	95,000
		By Prakash's Capital (Computer)		1,200
		By Loss transferred to :		
		Ravi's Capital A/c	1,100	
		Prakash's Capital A/c	1,100	2,200
	1,74,400			1,74,400

PARTNERS' CAPITAL ACCOUNTS

Dr. Cr.

Particulars	Ravi	Prakash	Particulars	Ravi	Prakash
	₹	₹		₹	₹
To Realisation A/c	8,000	1,200	By Balance b/d	30,000	10,000
To Realisation A/c (Loss)	1,100	1,100	By General Reserve	7,500	7,500
To Cash A/c (Bal. fig.)	30,400	15,200	By Realisation A/c (Realisation Exp.)	2,000	—
	39,500	17,500		39,500	17,500

CASH ACCOUNT

Dr. Cr.

Particulars	₹	Particulars	₹
By Balance c/d	25,000	By Realisation A/c	59,400
By Realisation A/c (Assets realised)	95,000	By Ravi's Loan A/c	15,000
		By Ravi's Capital A/c	30,400
		By Prakash's Capital A/c	15,200
	1,20,000		1,20,000

ILLUSTRATION 38.

Aman and Harsh were partners in a firm. They decided to dissolve their firm. Pass necessary journal entries for the following after various assets (other than Cash and Bank) and third party liabilities have been transferred to Realisation A/c.

(a) There was furniture worth ₹50,000. Aman took over 50% of the furniture at 10% discount and the remaining furniture was sold at 30% profit on book value.

(b) Profit and Loss Account was showing a credit balance of ₹15,000 which was distributed between the partners.

(c) Harsh's loan of ₹6,000 was discharged at ₹6,200.

(d) The firm paid realization expenses amounting to ₹5,000 on behalf of Harsh who had to bear these expenses.

(e) There was a bill for ₹1,200 under discount. The bill was received from Soham who proved insolvent and a first and final dividend of 25% was received from his estate.

(f) Creditors, to whom the firm owed ₹6,000, accepted stock of ₹5,000 at a discount of 5% and the balance in cash.

(g) The loss on dissolution was ₹8,000. *(I.S.C. 2014)*

SOLUTION:

JOURNAL

Date	*Particulars*		L.F.	*Dr.* (₹)	*Cr.* (₹)
(a)	Aman's Capital A/c	Dr.		22,500	
	Bank A/c	Dr.		32,500	
	To Realisation A/c				55,000
	(Half of the furniture taken over by Aman and the remaining half realised in Cash)				
(b)	Profit and Loss A/c	Dr.		15,000	
	To Aman's Capital A/c				7,500
	To Harsh's Capital A/c				7,500
	(Balance of Profit and Loss Account credited to the partners in their profit sharing ratio)				
(c)	Harsh's Loan A/c	Dr.		6,000	
	Realisation A/c	Dr.		200	
	To Bank A/c				6,200
	(Harsh's Loan of ₹6,000 discharged at ₹6,200)				
(d)	Harsh's Capital A/c	Dr.		5,000	
	To Bank A/c				5,000
	(Realisation expenses paid on behalf of Harsh)				
(e)	Realisation A/c	Dr.		1,200	
	To Bank A/c				1,200
	(Payment made to the bank from whom the bill was discounted)				
	Bank A/c	Dr.		300	
	To Realisation A/c				300
	(25% of the dishonoured bill recovered)				
(f)	Realisation A/c	Dr.		1,250	
	To Bank A/c				1,250
	(Stock accepted by Creditors and the balance amount paid in Cash)				

(g)	Aman's Capital A/c	Dr.		4,000	
	Harsh's Capital A/c	Dr.		4,000	
	To Realisation A/c				8,000
	(Transfer of loss on realisation)				

ILLUSTRATION 39.

Simar, Raja and Rita were partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1. The firm was dissolved on 31st March, 2019. After the transfer of assets (other than cash) and external liabilities to the Realisation Account, the following transactions took place :

(i) A debtor whose debt of ₹90,000 had been written off as bad, paid ₹88,000 in full settlement.

(ii) Creditors to whom ₹1,21,000 were due to be paid, accepted stock at ₹71,000 and the balance was paid to them by a cheque.

(iii) Raja had given a loan to the firm of ₹18,000. He was paid ₹17,000 in full settlement of his loan.

(iv) Investments were ₹53,000 out of which investments worth ₹43,000 were taken over by Simar at ₹52,000 and the balance of the investments were sold for ₹12,000.

(v) Expenses on dissolution amounted to ₹19,000 and the same were paid by the firm.

(vi) Profit on dissolution amounted to ₹30,000.

Pass the necessary journal entries for the above transactions in the books of the firm. *(C.B.S.E. 2020, Lucknow, Kolkata)*

SOLUTION :

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019 March 31					
(i)	Bank A/c	Dr.		88,000	
	To Realisation A/c				88,000
	(Bad debts earlier written off, now recovered)				
(ii)	Realisation A/c	Dr.		50,000	
	To Bank A/c				50,000
	(Payment made to creditors)				
(iii)	Raja's Loan A/c	Dr.		18,000	
	To Bank A/c				17,000
	To Realisation A/c				1,000
	(Raja's loan settled)				
(iv)	Simar's Capital A/c	Dr.		52,000	
	Bank A/c	Dr.		12,000	
	To Realisation A/c				64,000
	(Investments taken over by Simar and remaining sold)				

(v)	Realisation A/c Dr. To Bank A/c (Dissolution expenses paid by the firm)		19,000	19,000
(vi)	Realisation A/c Dr. To Simar's Capital A/c To Raja's Capital A/c To Rita's Capital A/c (Profit on dissolution credited to partners capital accounts)		30,000	12,000 12,000 6,000

Short Answer Questions

1. Give one distinction between reconstitution of a firm and dissolution of a firm.

Ans. In case of dissolution of a partnership (*i.e.*, reconstitution of a firm) the firm continues, while in case of dissolution of a firm, its business is discontinued.

2. What is the object of a Realisation Account in dissolution of partnership? *(I.S.C. 1997)*

Ans. The object of Realisation Account is to close the books of accounts and to determine the profit or loss on realisation of assets and payment of liabilities. The profit or loss disclosed by Realisation Account is transferred to Partner's Capital Accounts in their profit sharing ratio.

3. Mention two differences between dissolution of a partnership and dissolution of a firm. *(I.S.C. 1998)*

4. Mention the order in which the proceeds from the sale of Assets are utilised at the time of dissolution of partnership firm.

5. Why is the balance at bank never transferred to the Realisation Account on the dissolution of a partnership?

Ans. The purpose of opening a realisation account on the dissolution of the firm is to record the realisation of assets, payment of liabilities and determine the profit or loss on realisation. Cash at Bank is reliased asset and does not involve any profit or loss. Hence, it is not transferred to the Realisation Account.

6. How are the realisation expenses dealt with when a partnership firm is dissolved?

Ans. Following given are the various ways in which realisation expenses are dealt with when a partnership firm is dissolved :

(*a*) When realisation expenses are incurred — Realisation Account is debited and Bank Account is credited.

(*b*) When realisation expenses are paid by the partner on behalf of the firm—

Realisation A/c Dr.
To Partner's Capital A/c

(*c*) When as per agreement a partner is supposed to bear the expenses personally

(*i*) In case he pays such expenses : No Entry

(*ii*) In Case the expenses are paid out of the firm's bank account : Partner's Capital Account is debited and the Bank Account is credited.

7. Explain the accounting treatment at the time of dissolution of a partnership firm, of the assets and liabilities not already recorded in the books of the firm.

Ans. There may be some assets and liabilities, which have not been recorded in the books and thus do not appear in the Balance Sheet. The usual procedure of accounting treatment is :

(*i*) On the sale of unrecorded assets :

Cash/Bank A/c	Dr.	(With the amount realised on sale of unrecorded assets)
To Realisation A/c		

(*ii*) On payment of unrecorded liabilities :

Realisation A/c	Dr.	(With the amount paid for unrecorded liabilities)
To Bank A/c		

8. How should assets which are taken over by a partner be recorded in the partnership books on dissolution? *(I.S.C. 1996)*

9. On dissolution, what entry is passed if a partner takes over an asset of the firm valued ₹10,000 at ₹6,000?

Ans.

Partner's Capital A/c	Dr.	6,000	
To Realisation A/c			6,000

10. When an asset is taken over by a partner, why is his Capital Account debited?

Ans. When an asset is taken over by a partner, his Capital Account is debited because the claim of Capital Account is reduced by the value of the asset taken over.

11. When a liability is to be discharged by a partner, why is his Capital Account credited?

Ans. When a liability is to be discharged by a partner, his Capital Account is credited because the claim of the partner against the firm is increased by the amount of liability assumed.

12. Do you think that the loan by a partner is transferred to Realisation Account at the time of dissolution of a firm? Why?

Ans. No, it is not transferred to Realisation Account because its payment is made after the payment of all outside liabilities.

13. Do you think that the loan by a partner's relative is transferred to Realisation Account at the time of dissolution of a firm? Why?

Ans. Yes, it is transferred to Realisation Account because it is an outside liability.

14. How are debts of the firm and private debts dealt with in case of dissolution of partnership? *(I.S.C. 2004)*

Ans. According to section 49 of the Partnership Act, firm debts and private debts of the partners shall be settled as follows :

(*i*) The property of the firm shall be applied first for payment of firm's debts, and if there is any surplus, the share of each partner in the surplus shall be used to pay his private debts.

(*ii*) The private property of any partner shall be applied first for payment of his private debts, and if there is any surplus, it shall be used to pay the debts of the firm.

15. How is Workmen Compensation Reserve shown in the Balance Sheet of a partnership firm, treated at the time of its dissolution? *(I.S.C. 2013, 2016)*

Ans. Workmen Compensation Reserve to the extent of liability is Credited to Realisation A/c and the remaining amount of Workmen Compensation Reserve is Credited to the Partner's Capital A/cs in their profit sharing ratio. If there is no liability on account of Workmen Compensation, the entire amount is Credited to Partner's Capital A/cs.

16. How would you treat Employees Provident Fund shown on the liability side of balance sheet, at the time of dissolution of partnership firm and why? *(I.S.C. 2013)*

Ans. Employee's Provident Fund is a liability to the employees. Hence, it will be transferred to the credit side of Realisation Account and will be paid off.

17. Mention any two differences between Revaluation Account and Realisation Account. *(I.S.C. 2006; 2010; 2014; 2018)*

Ans. Distinction Between Revaluation Account and Realisation Account

No.	*Basis of distinction*	*Revaluation Account*	*Realisation Account*
1.	When prepared	This account is prepared on the admission, retirement or death of a partner.	This account is prepared on the dissolution of partnership firm.
2.	Object of preparation	This account is prepared to make necessary adjustments in the value of assets and liabilities.	This account is prepared to find out the profit or loss on the sale of assets and repayment of liabilities.

18. How will you deal with unrecorded assets and liabilities at the time of dissolution of a firm?

Ans. Unrecorded assets means assets which are not shown in the Balance Sheet. For example, Plant written off completely but do exist physically. Similarly, unrecorded liabilities means liabilities which are not shown in the Balance Sheet. These unrecorded assets and liabilities should not be transferred to the Realisation Account since they have no book value. Their accounting treatment is as follows :

(*i*)	When unrecorded asset is sold for Cash.	Cash/Bank A/c To Realisation A/c	Dr.	With realised value
(*ii*)	When unrecorded asset is taken over by a partner.	Partner's Capital A/c To Realisation A/c	Dr.	With agreed price
(*iii*)	When unrecorded liability is paid in Cash.	Realisation A/c To Cash/Bank A/c	Dr.	With actual payment
(*iv*)	When a partner agrees to settle unrecorded liability.	Realisation A/c To Partner's Capital A/c	Dr.	With agreed amount

19. On dissolution of the firm, partner A demands that his loan of ₹1,00,000 should be paid before payment of Capitals of the partners, whereas partners B and C demand that Capitals should be paid before the payment of A's loan. State the order of payment.

Ans. As per Section 48 of the Indian Partnership Act, 1932, partner's loan is paid before the payment of partner's Capitals.

20. A and B are partners in a firm sharing profits in the ratio of 3 : 2. Mrs. A has given a loan of ₹20,000 to the firm and the firm also obtained a loan of ₹10,000 from B. The firm was dissolved and its assets were realised for ₹25,000. State the order of payment of Mrs. A's Loan and B's Loan with reason, if there were no creditors of the firm.

Ans. As per Section 48 of the Indian Partnership Act, 1932, Mrs. A's Loan of ₹20,000 will be paid first and after that B's Loan will be paid up to the available amount of ₹5,000.

21. On dissolution of a firm, its Balance Sheet revealed total creditors ₹50,000; Total Capital ₹48,000; Cash Balance ₹3,000. Its assets were realised at 12% less. What will be loss on realisation?

Ans. ₹11,400

22. On dissolution of a firm, there was an Unrecorded asset of ₹2,000 which was taken over by a partner at ₹2,500. What entry will be passed?

Ans. Partner's Capital A/c	Dr.	2,500	
To Realisation A/c			2,500

23. In the Balance Sheet Total Debtors appear at ₹50,000 and Provision for Doubtful Debts appear at ₹1,500. How much amount will be realised from Debtors, if bad debts amount to ₹10,000 and remaining debtors are realised at a discount of 5%

Ans. ₹38,000

24. There was a contingent liability for B/R received from Ashok for ₹20,000 and discounted with the bank. Ashok became insolvent and 75 paise in a rupee were received from his estate. How much amount will be debited/credited to Realisation Account?

Ans. Debit ₹20,000 and Credit ₹15,000.

25. P, a partner, is to bear all expenses of realisation for which he is to be paid ₹2,000. P had to pay realisation expenses of ₹2,500. How much amount will be debited to Realisation Account?

Ans. ₹2,000

26. Total creditors amounted to ₹5,00,000. Investments valued ₹2,00,000 were not shown in the books. One of the creditors took over these investments in full satisfaction of his debt of ₹2,20,000. Remaining creditors were paid at 5% discount. Pass entry for payment.

Ans. Realisation A/c	Dr.	2,66,000	
To Cash/Bank A/c			2,66,000

27. Creditors amounting to ₹80,000 are transferred to Realisation Account. What entry will be made on their payment if ₹10,000 of the creditors are not to be paid and the remaining creditors agreed to accept 20% less amount?

Ans. Realisation A/c Dr. 56,000
To Cash/Bank A/c 56,000

28. X, Y and Z are partners in a firm in the ratio of 4 : 3 : 2. On firm's dissolution, firm's total assets are ₹70,000, creditors are ₹15,000. Realisation expenses are ₹2,100. Assets realised 15% more than the book-value. Creditors were paid 2% more. For profit/loss on realisation, Y's capital account will be debited/credited with how much amount?

Ans. Y's Account will be credited with ₹2,700.

29. The firm of Ravi and Mohan was dissolved on 31.3.2022. According to the agreement, Ravi had agreed to undertake the dissolution work for an agreed remuneration of ₹2,000 and bear all realisation expenses. Dissolution expenses were ₹1,500 and the same were paid by the firm.
Pass necessary Journal Entry for the payment of dissolution expenses.

Ans.

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
(*i*)	Realisation A/c	Dr.		2,000	
	To Ravi's Capital A/c				2,000
	(Remuneration due to Ravi)				
(*ii*)	Ravi's Capital A/c	Dr.		1,500	
	To Bank A/c				1,500
	(Realisation expenses paid on behalf of Ravi)				

30. Mohan and Kanwar are partners in a firm. Their firm was dissolved on 1.1.2022. Mohan was assigned the work of dissolution. For this work Mohan was to be paid ₹500. Mohan paid dissolution expenses of ₹400 from his own pocket. Will any Journal Entry be passed for ₹400 paid by Mohan? If yes, pass the entry. If no, give reason.

Ans.

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
	Realisation A/c	Dr.		400	
	To Mohan's Capital A/c				400
	(Dissolution expenses paid by Mohan on firm's behalf)				

Note : Mohan was not liable to bear the dissolution expenses.

31. How will the firm record the payment of realisation expenses which were to be borne by a partner, but paid by the firm on his behalf? *(ISC, 2015)*

Ans. Partner's Capital A/c Dr.
To Bank A/c
(Realisation expenses paid on behalf of the partner)

32. In settlement of Tarun's (a Partner) loan of ₹25,000 to the firm, a Computer not appearing the the books is taken over by him at an agreed value of ₹30,000. Pass necessary journal entry.

Ans.	Tarun's Loan A/c	Dr.	25,000	
	Tarun's Capital A/c	Dr.	5,000	
	To Realisation A/c			30,000
	(Tarun's loan of ₹25,000 settled by giving him unrecorded computer at an agreed value of ₹30,000)			

33. *C*'s Capital Account has a credit balance of ₹2,00,000; *C*'s Loan Account is showing a debit balance of ₹40,000. Bank Balance is ₹3,00,000. Show the treatment of *C*'s Loan A/c.

Ans.	*C*'s Capital A/c	Dr.	40,000	
	To *C*'s Loan A/c			40,000
	(*C*'s Loan transferred to *C*'s Capital A/c)			

34. At which value the assets against which provisions exist are transferred to Realisation Account?

Ans. Assets against which provision exist are transferred to Realisation Account at gross value.

35. What is the treatment of provisions against assets on dissolution of a firm?

Ans. Provisions against assets are credited to Realisation A/c.

36. What entry is passed when an asset is given to a Creditor in full settlement of his dues?

Ans. No Entry.

37. Provision for Depreciation ₹65,000; Provision for Doubtful Debts ₹30,000; and Provident Fund ₹1,50,000 has been transferred to the Credit side of Realisation Account. For which item payment is to be made by the firm?

Ans. Provident Fund.

38. Sundry Creditors ₹2,50,000 and Bills Payable ₹35,000 have been transferred to the Credit side of Realisation Account. Sundry Creditors were paid at a discount of 10%. What would be the further treatment if nothing else is mentioned?

Ans.	Realisation A/c	Dr.	35,000	
	To Bank A/c			35,000
	(Bills Payable paid off)			

39. State the reason why a partner's wife loan is transferred to Realisation A/c?

Ans. Wife Loan is an outside liability.

40. Why partner's loan is not transferred to Realisation A/c?

Ans. Partners' Loan is not an outside liability.

41. When a Creditor takes over an asset whose value is less than the amount due to him in full settlement of his claim, what entry shall be passed?

Ans. No entry.

42. Dissolution expenses amounting to ₹6,000 were to be borne by partner X and the balance by the firm. Dissolution expenses amounted to ₹15,000 and the entire amount was paid by firm. Pass journal entry.

Ans.

Realisation A/c	Dr.	9,000	
X's Capital A/c	Dr.	6,000	
To Bank A/c			15,000
(Dissolution expenses paid by the firm and X's share debited to his A/c.)			

43. Dissolution expenses amounting to ₹15,000 were to be borne by partner Y and the balance by the firm. Dissolution expenses amounted to ₹25,000 and the entire amount was paid by Y. Pass journal entry.

Ans.

Realisation A/c	Dr.	10,000	
To Y's Capital A/c			10,000
(Dissolution expenses paid by Y)			

44. Fixed Assets appear in the Balance Sheet of a firm at ₹52,000. They realised at a loss of 4% on net collection. State the amount collected from such assets.

Ans. If net collection is ₹100 loss will be ₹4 and hence book value of assets must be ₹104. As such, net amount realised from fixed assets will be : $\frac{100}{104}$ of ₹52,000 = ₹50,000

45. What will be the treatment of loan given to a partner by the firm at the time of its dissolution? *(I.S.C. 2017)*

Ans. Partner's Loan A/c will be debited to his Capital A/c.

46. State the Application of Assets as per Section 48 of the Indian Partnership Act, 1932. *(I.S.C. Sample paper 2017)*

Ans. Application of Assets. The amount realised from sale of assets (including the sum, if any, contributed by the partners to make up the deficiencies of capital) should be applied in the following manner and order :

(*a*) First of all, debts due to third parties are paid;

(*b*) Out of the remaining amount, loans advanced by partners are paid;

(*c*) Thereafter, balances of Partner's Capital Accounts are returned;

(*d*) If some amount still remains, it is distributed among the partners in their profit-sharing ratio.

47. State the order of payment of the following, in case of dissolution of partnership firm :

(*i*) to each partner proportionately what is due to him/her from the firm for advances as distinguished from capital (*i.e.*, partners' loan);

(*ii*) to each partner proportionately what is due to him on account of capital; and

(*iii*) for the debts of the firm to the third parties.

(C.B.S.E. Sample Paper 2020)

Ans. (*i*) for the debts of the firm to the third parties.

(ii) to each partner proportionately what is due to him/her from the firm for advances as distinguished from capital (*i.e.* partner' loan);

(iii) to each partner proportionately what is due to him on account of capital.

48. *P, Q* and *R* were partners with capitals of ₹3,00,000, ₹2,00,000 and ₹1,00,000 respectively. On dissolution it was found that there were 600 shares of ₹30 each in Gabriel Ltd., acquired at a cost of ₹24,000 and had been written off completely from the books. These shares are now valued at ₹60 each and divided among the partners in their profit sharing ratio. Give necessary Journal entry

[**Ans.**

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	P's Capital A/c	Dr.		12,000	
	Q's Capital A/c	Dr.		12,000	
	R's Capital A/c	Dr.		12,000	
	To Realisation A/c				36,000
	(600 shares valued at ₹60 each divided among partners)				

]

49. *B, C* and *D* were partners in a firm sharing profits and losses in the ratio of 1 : 4 : 5. On 31st March, 2018 the firm was dissolved and on that date the Balance Sheet of the firm showed a loan of ₹10,000 given by *C*'s brother *F*. *C* agreed to pay his brother's loan.

Pass necessary journal entry for the above on the firm's dissolution.

(C.B.S.E. 2019, Rajasthan)

Ans. JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Realisation A/c	Dr.		10,000	
	To C's Capital A/c				10,000
	(C's brother's loan taken over by C)				

50. At the time of dissolution of a partnership firm, the book value of sundry assets transferred to Realisation Account was ₹2,00,000. 50% of these sundry assets were taken by partner *A* at 20% discount, 40% of remaining assets were sold at a profit of 30% on cost. 5% of the balance was found obsolete and realised nothing. The remaining assets were taken over by a creditor in full settlement of his claim.

Pass necessary journal entry for the above. *(C.B.S.E. 2019, Delhi)*

Ans. JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	A's Capital A/c	Dr.		80,000	
	Bank A/c	Dr.		52,000	
	To Realisation A/c				1,32,000
	(Assets realised on dissolution)				

Q. 51. Name an item which is transferred to credit side of Realisation Account at the time of dissolution of partnership firm, but does not involve cash payment.
(C.B.S.E. 2020, Mumbai, Chennai)

Ans. Any one : Provision for Doubtful Debts; Accumulated Depreciation; Investment Fluctuation Fund.

Q. 52. Mention *any two* circumstances which can lead to dissolution of partnership.
(I.S.C. 2020)

Ans. The partnership is deemed to have been dissolved in any of the following cases :

(*i*) In case of change in the profit-sharing ratio of the existing partners
(*ii*) In case of admission of a new partner
(*iii*) In case of retirement of a partner
(*iv*) In case of expulsion of a partner
(*v*) In case of death of a partner
(*vi*) In case of insolvency of a partner
(*vii*) In case of expiry of the period of partnership

Q. 53. What is the status of the firm upon the dissolution of partnership?
(I.S.C. 2020)

Ans. In case of dissolution of partnership, the firm as a whole is not closed. It only results in the end of the old agreement and its replacement with the new agreement. The firm continues to carry on the business with a new agreement. Dissolution of partnership may or may not result into dissolution of partnership firm.

Objective Type Questions

State which of the following statements are true :

(*i*) There is no difference between the dissolution of partnership and dissolution of firm.

(*ii*) Loan from the wife of a partner is treated just like a loan from the partner himself.

(*iii*) Whenever the partnership changes, the old firm stands dissolved and a new firm comes into existence.

(*iv*) Partner's personal assets can also be used for payment of firm's liabilities.

(*v*) The firm will be necessarily dissolved, even if a single partner becomes insolvent.

(*vi*) Goodwill will be raised in the books of the firm on its dissolution.

(*vii*) Partner's loans have to be paid before any payment is made to any of the partners as capital.

(*viii*) A 'Revaluation Account' is opened on the dissolution of a firm.

(*ix*) On the dissolution of a firm, Goodwill will be sold like any other asset.

(*x*) On the dissolution of a firm, Realisation Account is debited with all the liabilities of the firm.

(*xi*) On the dissolution of a firm, cash-in-hand is transferrred to the 'Realisation Account'.

(*xii*) Profit on the dissolution of a firm is divided in the capital ratio.

(*xiii*) Dissolution of partnership automatically results in the dissolution of the firm.

Ans. True : (*iv*); (*vii*); (*ix*).

PRACTICAL QUESTIONS

(Question No. 1 to 36 are strictly in the serial order of Illustrations)

Q. 1. Manoj and Nand were partners sharing profits in the ratio of 3 : 2. Pass journal entries under following situations at the time of dissolution of firm :

(*i*) Workmen Compensation Reserve stood at ₹1,00,000 and there was no liability towards Workmen Compensation.

(*ii*) Workmen Compensation Reserve stood at ₹1,00,000 and liability in respect of it was acertained at ₹75,000.

(*iii*) Workmen Compensation Reserve stood at ₹1,00,000 and liability in respect of it was ascertained at ₹1,20,000.

(*iv*) Workmen Compensation Reserve stood at ₹1,00,000 and liability in respect of it was ascertained at ₹1,00,000.

Ans. (*i*) Dr. Workmen Compensation Reserve and Cr. Partner's Capital A/cs in 3 : 2.

(*ii*) Dr. Workmen Compensation Reserve and Cr. Realisation A/c by ₹75,000 and Partner's Capital A/cs by ₹25,000.

(*iii*) Dr. Workmen Compensation Reserve and Cr. Realisation A/c by ₹1,00,000.

(*iv*) Same as Case (*iii*)

Q.2. (*i*) Expenses of realisation ₹8,000.

(*ii*) Expenses of realisation ₹10,000 were paid by a partner.

(*iii*) Realisation expenses of ₹12,000 were to be met by Tushar, a partner, but were paid by the firm.

(*iv*) Suresh, a partner, was paid remuneration of ₹10,000 and he was to meet all expenses.

(*v*) Viru, a partner, was paid remuneration of ₹15,000 and he was to meet all expenses. Actual Expenses amounted to ₹20,000 which were paid by the firm.

(*vi*) Realisation expenses amounting to ₹15,000 were paid by the firm. ₹10,000 were to be borne by a partner and the balance by the firm.

(*vii*) Gauri, a partner, was allowed a remuneration of ₹25,000 and he was to meet all expenses. Firm paid an expense of ₹5,000.

Ans. (*i*) Debit Realisation A/c and Credit Bank A/c.

(*ii*) Debit Realisation A/c and Credit Partner's Capital A/c.

(*iii*) Debit Tushar's Capital A/c and Credit Bank A/c.

(*iv*) Debit Realisation A/c and Credit Suresh's Capital A/c.

(v) Debit Realisation A/c by ₹15,000, Debit Viru's Capital A/c by ₹5,000 and Credit Bank A/c by ₹20,000 and Credit Viru's Capital A/c by ₹15,000.

(vi) Debit Partner's Capital A/c by ₹10,000, Debit Realisation A/c by ₹5,000 and Credit Bank A/c by ₹15,000.

(vii) Debit Realisation A/c by ₹25,000; Credit Gauri's Capital A/c by ₹20,000 and Bank A/c by ₹5,000.

Q. 3. Pass necessary Journal Entries on the dissolution of a partnership firm in the following cases :

(i) *L*, a partner, was appointed to look after the dissolution process for which he was given a remuneration of ₹10,000.

(ii) Dissolution expenses ₹8,000 were paid by the partner, *M*.

(iii) Dissolution expenses were ₹5,000.

(iv) *P*, a partner, was appointed to look after the process of dissolution for which he was allowed a remuneration of ₹7,000. *P* agreed to bear the dissolution expenses. Actual dissolution expenses ₹4,000 were paid by *P*.

(v) *N*, a partner, was appointed to look after the process of dissolution for which he was allowed a remuneration of ₹9,000. *N* agreed to bear the dissolution expenses. Actual dissolution expenses ₹4,000 were paid by the firm.

(vi) *Q* a partner was appointed to look after the process of dissolution for which he was allowed a remuneration of ₹18,000. *Q* agreed to take over stock worth ₹18,000 as his remuneration. The stock had already been transferred to Realisation Account. *(C.B.S.E. 2016, Delhi)*

Ans. (i) Debit Realisation A/c and Credit *L*'s Capital A/c.

(ii) Debit Realisation A/c and Credit *M*'s Capital A/c.

(iii) Debit Realisation A/c and Credit Bank A/c.

(iv) Debit Realisation A/c and Credit *P*'s Capital A/c.

(v) Debit Realisation A/c by ₹9,000; Credit *N*'s Capital A/c by ₹5,000 and Bank A/c by ₹4,000.

(vi) No Entry.

Q. 4. Dipali and Rajshri are partners in a firm sharing profits and losses in the ratio of 3 : 2. They decided to dissolve their firm on 31st March, 2022, when their balance sheet was as under :

Liabilities		₹	*Assets*	₹
Capital Accounts :			Freehold Property	16,000
Dipali	17,500		Investments	4,000
Rajshri	10,000	27,500	Sundry Debtors	2,000
Sundry Creditors		2,000	Stock	3,000
Profit & Loss A/c		1,500	Cash at Bank	6,000
		31,000		31,000

Dipali took over the investments at an agreed value of ₹3,800, other assets were realised as follows : Freehold property ₹18,000; Sundry Debtors ₹1,800 and Stock ₹2,800.

Creditors of the firm agreed to accept 5% less. Expenses of realisation of assets amounted to ₹400. There was a type-writer in the firm bought out of the firm's money but the same has not been shown in the above balance sheet. The type-writer is now sold for ₹10,000.

Close the firm's books of accounts by preparing a realisation account, partners' capital accounts and bank account.

[**Ans.** Profit on realisation ₹11,100; Final payments to Dipali ₹21,260 and Rajshri ₹15,040; Total of Bank A/c ₹38,600.]

Q. 5. *A* and *B* were partners sharing profits and losses in 2 : 1. Their Balance Sheet as at 31st March, 2022 was as follows :

Liabilities		₹	*Assets*		₹
Sundry Creditors		2,10,000	Cash at Bank		60,000
A's Loan @12% p.a.		50,000	Sundry Debtors	1,80,000	
General Reserve		90,000	*Less* : Provision for		
A's Capital	4,00,000		Doubtful Debts	10,000	1,70,000
B's Capital	2,50,000	6,50,000	Stock		2,00,000
			Investments		1,50,000
			Plant & Machinery		4,00,000
			B's Loan		20,000
		10,00,000			10,00,000

Partners decide to dissolve the firm on the above date. Assets and liabilities realised as follows :

(*i*) Plant & Machinery was taken over by *A* at 60% of the book value.

(*ii*) Investments were taken over by *B* at 120%.

(*iii*) Sundry Creditors were paid off by giving them stock at 75% of the book value and the balance in cash.

(*iv*) Debtors realised 20% less of the amount due from them.

(*v*) *A*'s loan was paid off with interest for six months.

(*vi*) Realisation expenses amounted to ₹1,000.

You are required to prepare :

(*a*) Realisation Account

(*b*) *A*'s Loan Account and *B*'s Loan Account

(*c*) Partner's Capital Accounts, and

(*d*) Bank Account.

[**Ans.** Loss on Realisation ₹2,10,000; Final Payment to *A* ₹80,000 and *B* ₹10,000; Total of Bank Account ₹2,04,000.]

Hint : Payment to Sundry Creditors ₹60,000.

Q. 6. *A*, *B* and *C* were in partnership sharing profits in the ratio of 2 : 1 : 1. Their Balance Sheet showed the following position at the date of dissolution :

Liabilities		₹	Assets		₹
Creditors		40,000	Fixed Assets		50,000
Bills Payable		10,000	Stock		60,000
A's Loan		20,000	Debtors	30,000	
Mrs. *A*'s Loan		16,000	*Less* : Provision	2,000	28,000
Workmen Compensation Reserve		20,000			
Capitals :	*A*	40,000	Furniture		20,000
	B	20,000	Goodwill		18,000
	C	20,000	Cash at Bank		10,000
		1,86,000			1,86,000

I. *A* agreed to take over furniture at 20% less than the book value.

II. Fixed assets realised ₹32,000 and stock ₹55,000.

III. Bad Debts amounted to ₹5,000.

IV. Expenses of realisation were ₹3,000. Creditors were paid at a discount of 5%.

V. There was a claim of ₹6,400 for damages against the firm. It had to be paid.

Prepare necessary accounts.

[**Ans.** Loss on Realisation ₹55,400; Final payments: *A* ₹6,300; *B* ₹11,150; *C* ₹11,150; Total of Bank A/c ₹1,22,000.]

Hint : Nothing is mentioned in the question about the payment of B/P and Mrs. *A*'s Loan. It will be assumed that these will be paid in full.

Q. 7. The following was the Balance Sheet of *X*, *Y* and *Z* as at 28.2.2022 :

Liabilities		Amount	Assets	Amount
		₹		₹
Creditors		30,000	Bank	32,000
Bills Payable		10,000	Debtors	48,000
G's Loan		18,000	Stock	19,000
Y's Loan		20,000	Furniture	43,000
Workmen Compensation Reserve		33,000	Land and Building	1,09,000
Capitals :			*Z*'s Capital	20,000
X	75,000			
Y	85,000	1,60,000		
		2,71,000		2,71,000

The firm was dissolved on the above date on the following terms :

(*i*) Debtors realized ₹29,000 and creditors and bills payable were paid at a discount of 10%.

(*ii*) Stock was taken over by *X* for ₹17,000 and furniture was sold to *K* for ₹20,000.

(*iii*) Land and Building was sold for ₹2,98,000.

(*iv*) *G*'s loan was paid by a cheque of the same amount.

(*v*) Compensation to workmen paid by the firm amounted to ₹15,000.

Prepare Realisation Account, Capital Accounts and Bank Account.

[Ans. Profit on Realisation ₹1,49,000. Final Payments : Y's Loan ₹20,000; Capitals : X ₹1,13,667; Y ₹1,40,667; and Z ₹35,666. Total of Bank A/c ₹3,79,000.]

Hint. Workmen Compensation Reserve Credited to Realisation A/c ₹15,000 and to Capital Accounts ₹18,000.

Q. 8 (A). Pritam and Naresh decided to dissolve their firm on September 30, 2021, when their Balance Sheet stood as follows :

Liabilities	₹	*Assets*		₹
Capital Accounts :		Cash at Bank		400
Pritam	40,000	Stock-in-Trade		21,500
Naresh	20,000	Bills Receivable		8,800
Loan Accounts :		Sundry Debtors	45,000	
Naresh	14,000	*Less* : Provision for		
Mrs. Pritam	10,000	Bad Debts	1,500	43,500
Sundry Creditors	36,000	Furniture		3,000
Outstanding Rent	500	Plant & Machinery		23,000
		Goodwill		20,000
		Prepaid Insurance		300
	1,20,500			1,20,500

The assets were realised as follows :— Stock ₹20,000; Bills Receivable ₹3,800; Furniture ₹5,100; Plant & Machinery ₹35,000; Sundry Debtors at 10% less than book value.

Sundry Creditors allowed a discount of 5%. Pritam agreed to pay his wife's loan. Naresh agreed to pay outstanding rent. Expenses on dissolution came to ₹800.

Pritam and Naresh shared profits and losses in the ratio of their Capitals. Accounts were finally settled.

Prepare Journal, Realisation Account, Capital Accounts and Bank Account.

[Ans. Loss on Realisation ₹14,700 : Cash paid to Pritam ₹40,200 and Naresh ₹15,600; Total of Bank A/c ₹1,04,800.]

Hint : Goodwill and Prepaid Insurance will be debited to Realisation A/c and no further entry will be made in respect of these items.

Q. 8 (B). Mrs. Rita Chowdhary and Miss Shobha are partners in a firm, 'Fancy Garments Exports' sharing profits and losses equally. On 1st January, 2022, the Balance Sheet of the firm was as follows :

Liabilities	₹	*Assets*		₹
Sundry Creditors	75,000	Bank		36,000
Bills Payable	30,000	Stock		75,000
Mr. Chowdhary's Loan	15,000	Book Debts	66,000	
Reserve Fund	24,000	*Less*: Provision for		
Mrs. Rita Chowdhary's Capital	90,000	Doubtful Debts	6,000	60,000
Miss Shobha's Capital	30,000	Plant & Machinery		45,000
		Land & Buildings		48,000
	2,64,000			2,64,000

The firm was dissolved on the date given above. The following transactions took place:

(*i*) Mrs. Rita Chowdhary undertook to pay Mr. Chowdhary's Loan and took over 50 per cent of stock at a discount of 20 per cent.

(*ii*) Book-debts realised ₹54,000; balance of the stock was sold off at a profit of 30 per cent on cost.

(*iii*) Sundry Creditors were paid out at a discount of 10 per cent. Bills payable were paid in full.

(*iv*) Plant and Machinery realised ₹75,000 and Land and Buildings ₹1,20,000.

(*v*) Mrs. Rita Chowdhary took over the goodwill of the firm at a valuation of ₹30,000.

(*vi*) Realisation expenses were ₹5,250.

Show the Realisation Account, Bank Account and Partners' Capital Accounts in the books of the firm.

[**Ans.** Profit on realisation ₹1,32,000; Final Payments :— Rita ₹1,23,000 and Shobha ₹1,08,000, Total of Bank A/c ₹3,33,750.]

Q. 9. Anurag and Prem were partners sharing profits and losses in 2 : 1. On 31st March, 2020 their Balance Sheet was as follows :

Liabilities		₹	*Assets*		₹
Sundry Creditors		60,000	Bank		83,000
Mrs. Anurag's Loan		80,000	Sundry Debtors	60,000	
Anurag's Loan		50,000	*Less* : Provision for		
Workmen's Compensation			Doubtful Debts	3,000	57,000
Reserve		1,20,000	Stock		1,00,000
Investment Fluctuation Reserve		10,000	Furniture		20,000
Profit and Loss		5,000	Plant		4,00,000
Capitals :			Investments		45,000
Anurag	3,50,000		Advertisement Expenses		15,000
Prem	45,000	3,95,000			
		7,20,000			7,20,000

The firm was dissolved on the above date :

(*i*) Anurag took over 60% of the stock at a discount of 20%; 25% of the remaining stock was sold at a profit of 40% on cost; Remaining stock was found obsolete and realised nothing.

(*ii*) Firm had to pay ₹90,000 as compensation to workers.

(*iii*) Sundry Creditors took over investments in full settlement.

(*iv*) Sundry Debtors realised at 75% and plant realised 20% less.

(*v*) Prem agreed to take over the responsibility of completing dissolution work and he was given furniture as his remuneration.

(*vi*) Realisation expenses amounted to ₹10,000.

Prepare Realisation Account.

[**Ans.** Loss on Realisation ₹1,35,000.]

Hints : (*i*) Book value of remaining 25% stock : 25% of 40,000 = ₹10,000

Realised value of stock : $10,000 \times \frac{140}{100}$ = ₹14,000

(*ii*)

Workmen's Compensation Reserve A/c	Dr.	90,000	
To Realisation A/c			90,000
Realisation A/c	Dr.	90,000	
To Bank A/c			90,000

Workmen Compensation Reserve amounting to ₹30,000 will be transferred to the Cr. side of Capital Accounts.

(*iii*) There will be no entry of Sundry Creditors taking over the investments.

(*iv*) There will be no entry of Prem taking over furniture as his remuneration.

Q. 10. The following is the Balance Sheet of *A* and *B* as at 31st March, 2022 :

Liabilities	₹	*Assets*		₹
Mrs. *A*'s Loan	15,000	Cash		4,200
Mrs. *B*'s Loan	10,000	Bank		3,400
Trade Creditors	30,000	Debtors	30,000	
Bills Payable	10,000	*Less* : Provision	2,000	28,000
Outstanding Expenses	5,000	Investments		10,000
A : Capital	1,00,000	Stock		40,000
B : Capital	80,000	Truck		75,000
		Plant and Machinery		80,000
		B : Drawings		9,400
	2,50,000			2,50,000

Firm was dissolved on this date.

1. Half the stock was sold at 10% less than the book value and the remaining half was taken over by *A* at 20% more than the book value.

2. During the course of dissolution a liability under action for damages was settled at ₹12,000 against ₹10,000 included in the creditors.

3. Assets realised as follows :

Plant & Machinery — ₹1,00,000; Truck — ₹1,20,000; Goodwill was sold for ₹25,000; Bad Debts amounted to ₹5,000. Half the investments were sold at book value.

4. *A* promised to pay off Mrs. *A*'s Loan and took away half the investments at 10% discount.

5. Trade Creditors and Bills Payable were due on average basis of one month after 31st March, but were paid immediately on 31st March, at 12% discount per annum.

Prepare necessary accounts.

[**Ans.** Profit on Realisation ₹86,800; Final Payment to *A* ₹1,29,900 and *B* ₹1,14,000; Total of Bank A/c ₹3,00,600]

Hints : 1. Discount received on payment to Creditors $= 20{,}000 \times \frac{12}{100} \times \frac{1}{12} =$ ₹200

2. Discount received on payment to B/P $= 10{,}000 \times \frac{12}{100} \times \frac{1}{12} =$ ₹100

3. Cash balance of ₹4,200 has been transferred to the debit of Bank Account.

Q. 11. The following is the Balance Sheet of *A*, *B* and *C*, as at 31st March, 2022 :

Liabilities		₹	*Assets*		₹
Creditors		30,000	Bank		15,000
Mrs. *A*'s Loan		20,000	Bills Receivable		12,000
Outstanding Salary		8,000	Stock		40,000
Investment Fluctuation Fund		10,000	Sundry Debtors	40,000	
Reserves		12,000	*Less* : Provision for		
Capital Accounts :			Doubtful Debts	4,000	36,000
A	60,000		Land and Buildings		50,000
B	40,000		Furniture		10,000
C	20,000	1,20,000	Typewriters		7,000
			Investments		30,000
		2,00,000			2,00,000

The profit and loss sharing ratios of the partners are 3 : 2 : 1. At the above date, partners decide to dissolve the firm. The assets realised were as follows :

(*i*) Bills Receivable were realised at a discount of 5%. Debtors were all good; Stock realised ₹32,000. Land and Buildings realised at 40% higher than the book value.

(*ii*) Furniture was sold for ₹6,000 by auction and auctioneer's commission amounted to ₹300.

(*iii*) Typewriters were taken over by *A* for an agreed valuation of ₹5,000.

(*iv*) Investments were sold in the open market at a price of ₹25,000, for which a commission of 2% was paid to the broker.

(*v*) Creditors agreed to accept 10% less. All other liabilities were paid off at their book value.

(*vi*) The firm retrenched their employees three months before the dissolution of the firm and the firm had to pay ₹25,000 as compensation. This liability was not appearing in the above Balance Sheet.

Close the books of the firm by preparing Realisation Account, Partner's Capital Accounts, and Bank Account.

[**Ans.** Loss on Realisation ₹8,400; Final Payment to *A* ₹56,800; *B* ₹41,200 and *C* ₹20,600.]

Hint : Amount realised from Sundry Debtors : ₹40,000.

Q. 12 (A). Following is the Balance Sheet of Ramji Lal and Panna Lal as at 31st March, 2022 :

Liabilities	₹	*Assets*	₹
Capitals :		Goodwill	4,000
Ramji Lal	16,000	Machinery	6,000

Panna Lal	10,000	Plant		12,800
Reserves	3,600	Debtors	10,800	
Workmen Compensation Reserve	2,000	*Less* : Provision	800	10,000
Creditors	5,400	Bank		6,800
Bills Payable	2,600			
	39,600			39,600

They decided to dissolve the firm. Assets are realised as follows :

(*i*) Machinery 10% less than book value; Plant ₹12,500 and Goodwill ₹2,520.

(*ii*) Ramji Lal is to take over Debtors amounting to ₹6,800 at ₹6,000, remaining Debtors were realised for 90% of the book value.

(*iii*) One bill of ₹600 under discount having been dishonoured had to be taken up by them.

(*iv*) The Bill payable of ₹2,600 to be assumed by Panna Lal at that figure.

(*v*) Creditors are paid off at a discount of 10%.

(*vi*) An amount of ₹2,500 had to be paid for Workmen Compensation.

(*vii*) The liquidation expenses amounted to ₹400.

You are required to show the Realisation Account, Capital Accounts and Bank Account.

[**Ans.** Loss on Realisation ₹3,740; Amount paid to Ramji Lal ₹9,930; Amount paid to Panna Lal ₹12,530; Bank Account Total ₹30,820.]

Hint. Entire amount of Workmen Compensation Reserve of ₹2,000 will be Credited to Realisation Account.

Q. 12 (B). The following is the Balance Sheet of *A* and *B* as at 31st March, 2022 :

Liabilities	₹	*Assets*		₹
Sundry Creditors	30,000	Cash in Hand		500
Bills Payable	8,000	Cash at Bank		8,000
Mrs. *A*'s Loan	5,000	Stock in Trade		5,000
Mrs. *B*'s Loan	10,000	Investments		10,000
General Reserve	10,000	Debtors	20,000	
Investment Fluctuation Fund	1,000	*Less* : Provision	2,000	18,000
A's Capital	10,000	Plant & Machinery		20,000
B's Capital	10,000	Building		15,000
		Goodwill		4,000
		Profit & Loss A/c		3,500
	84,000			84,000

The firm was dissolved on 31st March, 2022 on the following terms :

(*a*) *A* promised to pay off Mrs. *A*'s loan and took away stock-in-trade at ₹4,000;

(*b*) *B* took away half of the investments at 10% discount;

(*c*) Debtors realised ₹19,000;

(*d*) Creditors and bills payable were due on an average basis of one month after 31st March, but they were paid immediately on 31st March, at 6% discount per annum;

(*e*) Plant realised ₹25,000, Building ₹40,000, Goodwill ₹6,000 and remaining investments at ₹4,500.

(*f*) There was an old typewriter in the firm which had been written off completely from the books. It is now estimated to realise ₹300. It was taken away by *B* at this estimated price;

(*g*) Realisation expenses were ₹1,000.

Prepare the necessary ledger accounts in the books of *A* and *B*.

[**Ans.** Profit on Realisation ₹31,490; Final Payments : *A* ₹29,995 and *B* ₹24,195; Total of Bank A/c ₹1,03,000.]

Hints : (1) Discount received on payment to Creditors $30{,}000 \times \frac{6}{100} \times \frac{1}{12} = ₹150$

(2) Discount received on payment to B/P $8{,}000 \times \frac{6}{100} \times \frac{1}{12} = ₹40$

(3) A Bank Account has been prepared in the question. Cash in hand balance of ₹500 has been transferred to the debit of Bank A/c.

Q. 13. Raman and Richa were partners in a firm sharing profits in the ratio of 7 : 3. On 31.3.2018 the Balance Sheet of the firm was as follows :

BALANCE SHEET OF RAMAN AND RICHA

as at 31.3.2018

Liabilities		₹	*Assets*	₹
Capitals :			Land and Building	7,50,000
Raman	7,00,000		Furniture	1,20,000
Richa	3,00,000	10,00,000	Debtors	1,32,000
Sundry Creditors		1,75,000	Stock	1,03,000
			Cash	70,000
		11,75,000		11,75,000

The firm was dissolved on 1.4.2018 and the assets and liabilities were settled as follows :

(*i*) Land and building was taken over by Raman at a depreciation of 10% for cash;

(*ii*) Creditors of ₹1,25,000 took over stock and debtors in full settlement of their claim;

(*iii*) Remaining creditors were paid by Richa;

(*iv*) Furniture realised ₹5,000 less than the book value.

(*v*) Expenses of realisation were ₹400.

Pass necessary journal entries for dissolution of the firm.

[**Ans.** Final Payment to Raman ₹5,66,720 and Richa ₹2,92,880]

Hints :

(*i*) Prepare Realisation A/c in Working Notes. Loss on Realisation will amount to ₹1,90,400.

(*ii*) No entry is to be passed for creditors taking over stock and debtors. Entry for remaining creditors taken paid by Richa :

Realisation A/c	Dr.	50,000	
To Richa's Capital A/c			50,000

Balance Sheet at the Date of Dissolution not Given

Q. 14. *A*, *B* and *C* are in partnership sharing in 4 : 3 : 3. They decided to dissolve the partnership firm. At the date of dissolution their creditors amounted to ₹16,800 and in the course of dissolution a contingent liability of ₹3,500 not brought into the accounts matured and had to be met. Their capitals stood at ₹12,000, ₹10,000 and ₹8,000 respectively. *B* had lent to the firm in addition to Capital ₹13,200. The assets realised ₹45,670.

Prepare the Realisation Account and partners' Capital Accounts. Also show the Bank Account.

[**Ans.** Sundry Assets ₹60,000; Loss on Realisation ₹17,830. Final payment to *A* ₹4,868; *B* ₹4,651; *C* ₹2,651. Total of Bank A/c ₹45,670.]

Q. 15. Ashok and Kishore were in partnership sharing profits in the ratio of 3 : 1. They agreed to dissolve the firm. The assets (other than cash of ₹2,000) of the firm realised ₹1,10,000. The liabilities and other particulars of the firm on that date were as follows :—

	₹	
Creditors	40,000	
Ashok's Capital	1,00,000	
Kishore's Capital	10,000	(Dr. balance)
Profit & Loss Account	8,000	(Dr. balance)
Realisation Expenses were	1,000	

Creditors were settled in full settlement at ₹38,000. Prepare Realisation and Cash Account.

[**Ans.** Book value of Assets (other than Cash) ₹1,20,000. Loss on Realisation ₹9,000. Final settlement : Kishore brings in ₹14,250 and Ashok is paid ₹87,250; Total of Cash A/c ₹1,26,250.]

Q. 16. *X* and *Y* were partners in a firm sharing profits and losses in the ratio of 5 : 3. They agreed to dissolve the firm on June 30, 2022. On that date, the Capitals of *X* and *Y* were ₹80,000 and ₹40,000 respectively; the amount owed by *X* to the firm was ₹32,000 and the amount owed by the firm to *Y* was ₹25,000; the creditors amounted to ₹37,000 and balance at bank ₹10,000. The assets other than the amount owing by *X* to the firm realised ₹46,000. Realisation expenses amounted to ₹2,000. Prepare the Balance Sheet of the firm as on June 30, 2022 and necessary ledger accounts to close the books of the firm.

[**Ans.** Sundry Assets (other than Cash and *X*'s loan) ₹1,40,000; Loss on Realisation ₹96,000; Cash brought in by *X* ₹12,000; Payment to *Y* ₹4,000; Total of Bank A/c ₹68,000.]

Note : ₹32,000 owed by *X* will be transferred to the debit side of his Capital Account.

Q. 17. On 1st April, 2017, *A*, *B* and *C* commenced business in partnership sharing profit and losses in proportion of 1/2, 1/3 and 1/6 respectively. They paid into their Bank A/c as their capital ₹22,000 being ₹10,000 by *A*, ₹7,000 by *B* and ₹5,000 by *C*. During the year they drew ₹5,000, being ₹1,900 by *A*, ₹1,700 by *B* and ₹1,400 by *C*.

On 31st March, 2018, they dissolved their firm. *A* taking up stock at an agreed valuation of ₹5,000, *B* taking up furniture at ₹2,000 and *C* taking up debtors at ₹3,000. After paying up their creditors, there remained a balance of ₹1,000 at Bank. Prepare the necessary accounts showing the distribution of the cash at the Bank and of the further cash brought in by any partner as the case required.

[**Ans.** Sundry Assets ₹17,000. Loss on Realisation ₹6,000; Amount paid to *A* ₹100; Amount paid to *B* ₹1,300. Amount brought in by *C* ₹400; Total of Bank A/c ₹1,400.]

Q. 18. *X*, *Y* and *Z* entered into partnership on 1st October, 2021 sharing profits and losses in the proportions of 4 : 3 : 2, respectively, and with capitals of ₹30,000, ₹20,000 and ₹10,000.

Their assets and liabilities on 1st October, 2022, the date on which they decided to wind up their affairs, were as follows :

Office Fixtures ₹1,000; Debtors ₹28,000; Bills Receivable ₹5,000; and Stock-in-trade ₹45,000. Sundry creditors were ₹30,000; Bills Payable ₹4,000.

X agreed to take over the Stock-in-trade at a discount of 10% and pay off the Bills Payable.

Y agreed to take over the Book Debts at a discount of 20% and pay off the Creditors.

Z took over the Bills Receivable at ₹4,877 and Office Fixtures at a depreciation of 10%.

5% p.a. interest is to be credited to each partner on his capital.

Prepare Realisation a/c and Capital a/cs of the partners and an account showing adjustment of profits or losses in the business.

[**Ans.** Loss (P & L A/c Dr. Balance) ₹15,000; Realisation loss ₹10,323; Cash brought in by *X* ₹17,755 and *Z* ₹1,404; Cash paid to *Y* ₹19,159.]

Hint : Interest on Capital will not be allowed, because there is loss in the business.

Q. 19. *P*, *Q* and *R* started business on 1st April, 2021. They shared profit and loss in the ratio of 2 : 2 : 1. Capitals contributed by them were *P* ₹40,000; *Q* ₹30,000 and *R* ₹20,000. The partners were entitled to interest on capital @ 6% p.a.

During the year the firm earned a profit (before interest) of ₹25,000. The partners had withdrawn *P* ₹10,000; *Q* ₹8,000 and *R* ₹5,000.

On 31st March, 2022 the firm was dissolved. The assets realised ₹1,00,000. The creditors of ₹15,000 were paid at a discount of 3%. Expenses incurred on realisation were ₹1,450.

Prepare Partners' Capital Accounts, Realisation Account, Cash Account, Profit and Loss Appropriation Account and Balance Sheet to close the books of the firm.

[**Ans.** Divisible profits ₹19,600; Capital A/cs on 31-3-2022 before dissolution *P* ₹40,240; *Q* ₹31,640; *R* ₹20,120. Total Sundry Assets ₹1,07,000, Loss on Realisation ₹8,000, Final payments : *P* ₹37,040; *Q* ₹28,440 and *R* ₹18,520. Total of Cash A/c ₹1,00,000.]

Q. 20. *A*, *B* and *C* were partners from 1st April 2020 with capitals of ₹3,00,000; ₹2,00,000 and ₹1,50,000 respectively. They shared profits in the ratio of 2 : 2 : 1. They carried on business for two years. In the first year ending on 31st March, 2021, they made a profit of ₹2,00,000 but in the second year ending on 31st March, 2022, a loss of ₹60,000 was incurred. As the business was no longer profitable they dissolved the firm on 31st March, 2022. Creditors on that date were ₹75,000. The partners withdrew for personal use ₹40,000 per partner per year. The assets realised ₹4,00,000. The expenses of realisation were ₹5,000.

Prepare Realisation Account and show your workings clearly.

[**Ans.** Balances of Capital A/cs before Dissolution *A* ₹2,76,000; *B* ₹1,76,000 and *C* ₹98,000; Total Assets ₹6,25,000; Loss on Realisation ₹2,30,000.]

Q. 21. *M, N* and *O* were partners in a firm sharing profits and losses in the ratio of 1/2 : 1/3 : 1/6 respectively. They agreed to dissolve their firm on 31st March, 2022 at which date their Balance Sheet was as under :

Liabilities		₹	*Assets*		₹
Capital Accounts :			Machinery		1,21,500
M	1,05,000		Stock		22,650
N	50,000	1,55,000	Investments		44,490
Mrs. *M*'s Loan		30,500	Debtors	27,900	
Creditors		55,000	*Less* : Provision	1,800	26,100
Workmen's Compensation Fund		48,000	*O*'s Capital		39,500
			Cash at Bank		16,260
			Advertisement Suspense Account		18,000
		2,88,500			2,88,500

The investments are taken over by *M* for ₹52,500. *M* agrees to discharge the loan of his wife. *N* takes over all the stock at ₹21,000 and debtors amounting to ₹15,000 at ₹12,000. Machinery is sold for ₹2,01,000. The remaining debtors realise 50% of the book value. The expenses of realisation amounted to ₹1,800. The investments of the value of ₹9,000 were not recorded in the books. These were taken over by the creditors.

Prepare the Realisation A/c, Bank A/c and the Capital A/cs of the partners closing the books of the firm.

[**Ans.** Profit on Realisation ₹85,410; Cash brought in by *O* ₹20,265; Payment made to *M* ₹1,40,705; and to *N* ₹55,470; Total of Bank A/c ₹2,43,975.]

Hints :

(1) No compensation is payable to workmen. Hence, the entire amount of Workmen's Compensation Fund will be credited to partner's capital accounts in their profit sharing ratio.

(2) Advertisement Suspense Account is a fictitious asset. It will be debited to capital accounts.

(3) No separate entry will be made for unrecorded investments of ₹9,000. Creditors will be paid ₹46,000 (*i.e.* ₹55,000 *less* ₹9,000).

Q. 22 (A). Following is the Balance Sheet of Deepak and Jyoti, who were sharing profit and losses in the ratio of 3 : 2, as at March 31, 2022 :

Liabilities		₹	*Assets*		₹
Creditors		38,000	Cash		1,500
Mrs. Deepak's Loan		10,000	Bank		10,000
Bank Loan		15,000	Debtors	20,000	
Capital A/cs:			*Less* : Provision for		
Deepak	10,000		Doubtful Debts	1,000	19,000
Jyoti	8,000	18,000	Stock		12,000
Current A/cs:			Furniture		6,000
Deepak	2,000		Plant		30,000
Jyoti	500	2,500	P & L A/c (Dr. Balance)		5,000
		83,500			83,500

The firm was dissolved on that date and the following arrangements were made:—

(*i*) Assets realised as follows : Debtors ₹18,000; Furniture ₹5,500; Plant ₹32,000.

(*ii*) Deepak agreed to take over stock in full settlement of his wife's loan.

(*iii*) Creditors were paid at 2% discount and Bank Loan was discharged along with interest due for six months @ 10% p.a. and

(*iv*) Expenses of realisation amounted to ₹1,800.

Show the necessary ledger accounts to close the books of the firm.

[**Ans.** Loss on Realisation ₹3,290; Final Payments : Deepak ₹7,026 and Jyoti ₹5,184; Total of Cash/Bank A/c ₹67,000.]

Hint : There will be no entry for the payment of Mrs. Deepak's Loan.

Q. 22 (B). *A*, *B* and *C* sharing profits in the proportion of 3 : 2 : 1 agreed upon dissolution of their partnership firm on 31st March, 2022 at which date their balance sheet was as under :

Liabilities		₹	*Assets*		₹
Capital A/cs :			Machinery		40,500
A	40,000		Stock-in-Trade		7,550
B	20,000	60,000	Investments		20,830
Mrs. *A*'s Loan		10,000	Debtors	9,300	
Creditors		18,500	*Less* : Provision for		
Investments Fluctuation Fund		6,000	Doubtful Debts	600	8,700
			Current A/c—'*C*'		11,500
			Cash at Bank		5,420
		94,500			94,500

The investments are taken over by *A* for ₹17,500. *A* agrees to discharge his wife's loan. *B* takes over all the Stock at ₹7,000 and debtors amounting to ₹5,000 at ₹4,000. Machinery is sold for ₹67,000. The remaining debtors realise 50% of book value. The expenses of realisation amount to ₹600.

It is found that an investment not recorded in the books is worth ₹3,000 and it is taken over by one of the creditors at this value.

Show the necessary ledger accounts on completion of the dissolution of firm.

[**Ans.** Profit on realisation ₹28,470; Cash brought in by *C* ₹6,755; Payment to *A* ₹46,735 and *B* ₹18,490. Total of Bank A/c ₹81,325.]

Hint : *C*'s Current A/c appears on the assets side, which means that it has a debit balance. As such, it will be transferred to the Debit side of *C*'s Capital Account.

Q. 23. Mehta and Menon were partners in a firm, sharing profits and losses in the ratio of 7 : 3.

They decided to dissolve their partnership firm on 31st March, 2016. On that date, their books showed the following ledger account balances :

	₹
Sundry Creditors	27,000
Profit and Loss A/c (Dr.)	8,000
Cash in Hand	6,000
Bank Loan	20,000
Bills Payable	5,000
Sundry Assets	1,98,000
Capital A/cs :	
Mehta	1,12,000
Menon	48,000

Additional Information :

(*a*) Bills Payable falling due on 31st May, 2016 were retired on the date of dissolution of the firm, at a rebate of 6% per annum.

(*b*) The bankers accepted the furniture (included in sundry assets) having a book value of ₹18,000 in full settlement of the loan given by them.

(*c*) Remaining assets were sold for ₹1,50,000.

(*d*) Liability on account of outstanding salary not recorded in the books, amounting to ₹15,000 was met.

(*e*) Menon agreed to take over the responsibility of completing the dissolution work and to bear all expenses of realization at an agreed remuneration of ₹2,000. The actual realization expenses were ₹1,500 which were paid by the firm on behalf of Menon.

You are required to prepare :

(*i*) Realisation Account, and

(*ii*) Partners' Capital Accounts. *(I.S.C. 2017)*

[**Ans.** Loss on Realisation ₹44,950; Final Payment to Mehta ₹74,935 and Menon ₹32,615.]

Hints : (*i*) There will be no entry for payment of Bank Loan.

(*ii*) Entry for remuneration and realisation expenses :

Realisation A/c	Dr.	2,000	
To Menon's Capital A/c			500
To Cash A/c			1,500

Q. 24 (A). *X, Y* and *Z* were in partnership sharing profits and losses in the ratio of 7 : 2 : 1 and the Balance Sheet of the firm stood at 31st March, 2022, as under:—

Liabilities		₹	*Assets*	₹
Creditors		3,142	Cash in Hand	244
Provision for Depreciation			Debtors	1,746
on Machinery		4,000	Stock	3,498
Capital Accounts :			100 Shares in *B* Co. Ltd.	2,000
X	3,582		60 Shares in *C* Co. Ltd.	480
Y	2,720		Patents	7,600
Z	16,124	22,426	Machinery	6,000
			Buildings	5,000
			Goodwill	3,000
		29,568		29,568

On 31st March, 2022, it was decided to dissolve the firm on the following terms:

(*i*) *X* is to take over the buildings at ₹7,300.

(*ii*) *Y*, who will continue with business, to take over Goodwill, Stock and Debtors at book values, Patents at ₹6,500 and Machinery at ₹1,500. He also agreed to pay the Creditors.

(*iii*) *Z* agreed to take the shares in *C* Co. Ltd. at ₹5 each.

(*iv*) The shares in *B* Co. Ltd. to be divided in profit sharing ratio.

Show the ledger accounts to record the dissolution.

[**Ans.** Profit on realisation ₹520; Cash brought in by *X* 4,754 and *Y* ₹10,678; Final payment to *Z* ₹15,676: Total of Cash A/c ₹15,676.]

Q. 24 (B). Following is the balance sheet of *P, Q* and *R* who were sharing profits and losses in the ratio of 3 : 2 : 1.

Liabilities	₹	*Assets*		₹
Bank Balance	12,000	Debtors	20,000	
Creditors	70,000	*Less* : Provision	1,200	18,800
Mrs. *P*'s Loan	25,800	Stock		40,000
Capital Accounts :		3,000 Shares in '*A*' Ltd.		30,000
P	1,20,000	Motor Car		75,000
Q	95,000	Plant		80,000
R	5,000	Advertisement Suspense A/c		84,000
	3,27,800			3,27,800

The firm was dissolved on that date and the following arrangements were made:

I. Assets realised as follows: Debtors ₹15,000; Plant at 30% discount.

II. Stock was valued at ₹36,000 and this was taken over by *P* and *Q* equally.

III. Market value of the shares of *A* Ltd. is ₹16 per share. Half the shares were sold in the market and the balance half were taken over by *P* and *Q* in their profit sharing ratio.

IV. A creditor for ₹50,000 took over Motor Car in full settlement of his claim and the balance of creditors were paid at a discount of 2%.

V. Expenses of realisation amounted to ₹6,000. *P* agreed to discharge his wife's Loan.

Prepare Journal entries and Ledger accounts.

[**Ans.** Loss on Realisation ₹44,400. *R* brings in ₹16,400; Final payment to *P* ₹49,200 and *Q* ₹24,600. Total of Bank A/c ₹1,11,400.]

Q. 25. *P*, *Q* and *R* were partners in a firm sharing profits in the ratio of 1 : 2 : 2. Their Balance Sheet as at 31st March, 2019 was as follows :

BALANCE SHEET OF *P*, *Q* AND *R*

as at 31st March, 2019

Liabilities		₹	*Assets*		₹
Creditors		2,10,000	Land and Buildings		5,00,000
Bank Overdraft		50,000	Office Equipment		8,000
Q's Loan		40,000	Stock		2,00,000
Capitals :			Debtors	60,000	
P	1,00,000		*Less* : Provision for Doubtful Debts	3,000	57,000
Q	2,00,000				
R	2,00,000	5,00,000	Bank		35,000
		8,00,000			8,00,000

Partners agreed to dissolve the firm on that date. You are given the following information about dissolution :

(*i*) One of the Debtors for ₹20,000 paid ₹12,000 in full settlement of his account and debtors of ₹5,000 were proved bad.

(*ii*) Part of the stock was sold for ₹20,000 (being 25% more than the book value).

(*iii*) Office Equipment was accepted by the creditor for ₹7,000 in full settlement. Another creditor of ₹40,000 was paid only 40% in full settlement of his account and remaining creditors accepted remaining stock in full settlement of their account.

(*iv*) An unrecorded asset of ₹20,000 was handed over to an unrecorded liability of ₹15,000 in full settlement.

(*v*) Land & Buildings were sold at a loss of 20%.

(*vi*) *Q*'s Loan was settled by payment of ₹30,000.

(*vii*) Realistion expenses ₹16,000 were paid by *R*.

You are required to prepare the necessary accounts.

[**Ans.** Loss on Realisation ₹1,10,000; Final Payment to *P* ₹78,000; *Q* ₹1,56,000 and *R* ₹1,72,000; Total of Bank A/c ₹5,02,000.]

Hints : (*i*) There will be no entry for unrecorded asset given to unrecorded liability.

(*ii*) Entry for payment of *Q*'s Loan will be :

Q's Loan A/c	Dr.	40,000	
To Bank A/c			30,000
To Realisation A/c			10,000

Q. 26. *A*, *B* and *C* were partners in a firm sharing profits & losses in the ratio of 2 : 2 : 1. The Balance Sheet of the firm at the date of dissolution was as follows:

Liabilities	₹	*Assets*	₹
Bank Overdraft	21,000	Debtors	40,000
Creditors	86,000	Stock	60,000
Provident Fund	18,000	Investments	25,000
Capital Accounts :		Machinery	80,000
A	1,05,000	Prepaid Expenses	3,200
B	42,000	Goodwill	38,800
		C's Capital Account	25,000
	2,72,000		2,72,000

You are informed that :

(1) They appointed *B* to realise the assets. He is to receive 5% of the amounts realised from Debtors, Stock and Machinery, and is to bear all expenses of realisation.

(2) Bad Debts amounted to ₹2,000; Stock realised ₹36,000 and Machinery realised ₹46,000. There was an unrecorded asset of ₹10,000 which was taken over by *A* at ₹8,000.

(3) Market value of Investments was ascertained to be ₹20,000, and one of the creditors agreed to accept the Investments at this value. Remaining creditors were paid at a discount of ₹6,000.

(4) An office typewriter, not shown in the books of accounts, realised ₹20,000.

(5) There were outstanding expenses amounting to ₹6,000. These were settled for ₹4,500. Expenses of realisation met by *B* amounted to ₹2,000.

Prepare necessary accounts.

[**Ans.** Loss on Realisation ₹83,500; *C* brings in ₹41,700; Final payment to *A* ₹63,600; and *B* ₹14,600. Total of Bank A/c ₹1,81,700.]

Q. 27. *A*, *B* and *C* were in partnership sharing profit and losses in the ratio of 1 : 2 : 2. Their Balance Sheet at 31st March, 2022 was as under :

Liabilities		₹	*Assets*	₹
Sundry Creditors		50,000	Goodwill	40,000
Capital Accounts :			Building	2,80,000
A	1,00,000		Patents	18,000
B	1,50,000		Investments	25,000
C	1,40,000	3,90,000	Stock	40,000

Current Account : *A*	20,000	Bills Receivable		8,000
		Debtors	24,800	
		Less : Provision	1,200	23,600
		Cash at Bank		4,800
		Current Accounts :		
		B	8,400	
		C	12,200	20,600
	4,60,000			4,60,000

C died on 1st April, 2022 and it was decided to dissolve the firm. The following transactions took place :

(*i*) An unrecorded asset was realised for ₹50,000.

(*ii*) *B* took over half the investments at 10% discount and *C* took over Bills Receivable at 20% discount.

(*iii*) Stock realised as follows :
60% of the stock was realised in full.
10% of the stock was realised at a discount of 20%.
Remaining stock was realised at a profit of 20%.

(*iv*) Building realised ₹2,50,000; Debtors ₹20,000; Goodwill Nil and remaining investments ₹10,000.

(*v*) Discount of ₹1,600 was allowed by creditors.

(*vi*) A contingent liability, not brought into the account, was settled for ₹2,000.

You are required to prepare necessary accounts.

[**Ans.** Loss on Realisation ₹45,750; Final Payments *A* ₹1,10,850; *B* ₹1,12,050 and *C* ₹1,03,100; Total of Bank A/c ₹3,76,400.]

Hint : Stock realised ₹41,600.

Q. 28. *A*, *B* and *C* are partners sharing profits and losses in the ratio of 4 : 2 : 1. On 31st March, 2022, their Balance Sheet was as follows :

Liabilities		₹	*Assets*		₹
Sundry Creditors		35,400	Goodwill		12,700
Mrs. *B*'s Loan		15,000	Leasehold Premises		1,00,000
Capital Accounts :			Plant and Machinery		60,000
A	1,30,000		Stock		60,000
B	1,02,700		Sundry Debtors	30,000	
C	5,000	2,37,700	*Less* : Provision	700	29,300
			Cash at Bank		17,700
			Profit & Loss A/c		8,400
		2,88,100			2,88,100

It was decided to dissolve the firm, *A* agreeing to take over the business (except Cash at Bank) at the following valuations :

Leasehold Premises at ₹60,000

Plant and Machinery at ₹12,000 less than the book value.

$\frac{1}{4}$th stock at $33\frac{1}{3}\%$ more than its book value.

Remaining Stock at 20% more than the book value.

Sundry Debtors subject to a provision of 5%.

Mrs. *B*'s Loan was paid in full and the creditors were proved at ₹32,000 and were taken over by *A*. Expenses of dissolution came to ₹900.

Prepare necessary accounts to close the books of the firm and prepare the Balance Sheet of *A*.

[**Ans.** Loss on Realisation ₹49,000; Cash brought in by *A* ₹81,300 and by *C* ₹3,200; Cash paid to *B* ₹86,300; Total of Cash A/c ₹1,02,200; B/S Total ₹2,10,500.]

Q. 29. Give journal entries in each of the following alternative cases on the dissolution of a firm :

(*i*) Realisation expenses paid by *X* on behalf of the firm.

(*ii*) Realisation expenses paid by the firm ₹1,000. However, the expenses were to be borne by partner *X* for which he was to be given a commission of 5% on net cash realised on dissolution. Cash realised from assets was ₹2,00,000 and cash paid for liabilities was ₹40,000.

(*iii*) General Reserve appearing in the balance sheet was ₹20,000.

(*iv*) Sundry Creditors amounted to ₹15,000. These were paid at a discount of 2%.

[**Ans.** (*i*) Debit Realisation A/c and Credit *X*'s Capital A/c.

(*ii*) Debit *X*'s Capital A/c and Credit Bank A/c by ₹1,000;
Debit Bank A/c and Credit Realisation A/c by ₹2,00,000;
Debit Realisation A/c and Credit Bank A/c by ₹40,000;
Debit Realisation A/c and Credit *X*'s Capital A/c by ₹8,000.

(*iii*) Debit General Reserve A/c and Credit Partner's Capital A/cs in profit sharing ratio.

(*iv*) Debit Realisation A/c and Credit Bank A/c by ₹14,700.]

Q. 30. Jain, Sharma and Verma were partners in a firm sharing profits in the ratio of 1 : 2 : 1. On 31st March, 2018 their firm was dissolved. It was agreed that Sharma will look after the dissolution work and will be paid ₹15,000 as remuneration. The dissolution expenses were ₹5,000. ₹2,84,000 were paid to the creditors in full settlement of their claim of ₹3,00,000. Dissolution of the firm resulted into a loss of ₹18,000.

Pass necessary journal entries for the above transactions. (*C.B.S.E. 2019, Kerala*)

[**Ans.** (*a*) Debit Realisation A/c and Credit Sharma's Capital A/c by ₹15,000.

(*b*) Debit Realisation A/c and Credit Bank A/c by ₹5,000.

(*c*) Debit Realisation A/c and Credit Bank A/c by ₹2,84,000.

(*d*) Debit Partners Capital A/cs respectively by ₹4,500, ₹9,000 and ₹4,500 and Credit Realisation A/c by ₹18,000.]

Q. 31. Gaurav, Saurabh and Vaibhav were partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1. They decided to dissolve the firm on 31st March, 2018. After transferring Sundry assets (other than cash in hand and cash at Bank) and third party liabilities to realisation account, the assets were realized and liabilities were paid off as follows :

(*i*) A machinery with a book value of ₹6,00,000 was taken over by Gaurav at 50% and stock worth ₹5,000 was taken over by a creditor of ₹9,000 in full settlement of his claim.

(*ii*) Land and building (book value ₹3,00,000) was sold for ₹4,00,000 through a broker who charged 2% commission.

(*iii*) The remaining creditors were paid ₹76,000 in full settlement of their claim and the remaining assets were taken over by Vaibhav for ₹17,000.

(*iv*) Bank loan of ₹3,00,000 was paid along with interest of ₹21,000.

Pass necessary journal entries for the above transactions in the books of the firm.

(C.B.S.E. 2019, M.P.)

[**Ans.** (*i*) Debit Gaurav's Capital A/c and Credit Realisation A/c by ₹3,00,000.

(*ii*) Debit Bank A/c and Credit Realisation A/c by ₹3,92,000.

(*iii*) (*a*) Debit Realisation A/c and Credit Bank A/c by ₹76,000.
(*b*) Debit Vaibhav's Capital A/c and Credit Realisation A/c by ₹17,000.

(*iv*) Debit Realisation A/c and Credit Bank A/c by ₹3,21,000.]

Q. 32. Adiraj and Karan were partners in a firm sharing profits and losses in the ratio 3 : 2. On 31st March, 2018 the firm was dissolved. After the transfer of assets (other than cash in hand and at bank) and third party liabilities to the Realisation Account, the following information was provided :

(*i*) Furniture of ₹70,000 was sold for ₹68,000 by auction and auctioneer's commission amounted to ₹2,000.

(*ii*) Adiraj's loan amounting to ₹35,000 was settled at ₹37,500.

(*iii*) Out of the stock of ₹80,000, Karan took over 50% of the stock at a discount of 20% while the remaining stock was sold off at a profit of 30% on cost.

(*iv*) A bills receivable of ₹3,000 under discount was dishonoured as the acceptor had become insolvent and hence the bill had to be met by the firm.

(*v*) Profit and Loss Account showed a debit balance of ₹56,000.

(*vi*) Realization expenses amounted to ₹2,000 which were paid by Adiraj.

Pass the necessary journal entries for the above transactions on the dissolution of the firm.

(C.B.S.E. 2019, Chennai)

[**Ans.** (*i*) Debit Bank A/c and Credit Realisation A/c by ₹66,000.

(*ii*) Debit Adiraj's Loan A/c by ₹35,000 and Realisation A/c by ₹2,500 and Credit Bank A/c by ₹37,500.

(*iii*) Debit Karan's Capital A/c by ₹32,000 and Bank A/c by ₹52,000 and Credit Realisation A/c by ₹84,000.

(*iv*) Debit Realisation A/c and Credit Bank A/c by ₹3,000.

(*v*) Debit Partners Capital A/cs by ₹33,600 and ₹22,400 and Credit P&L A/c by ₹56,000.

(*vi*) Debit Realisation A/c and Credit Adiraj's Capital A/c by ₹2,000.]

Q. 33. Give the necessary journal entries for the following transactions on dissolution of the firm of Aman and Rajat on 31st March, 2016, after the transfer of various assets (other than cash) and the third party liabilities to Realisation Account. They shared profits and losses in the ratio of 2 : 1.

(*a*) There was a bill of exchange of ₹10,000 under discount. The bill was received from Derek who became insolvent.

(*b*) Bills Payable of ₹30,000 falling due on 30th April, 2016 was discharged at ₹29,550.

(*c*) Creditors of ₹30,000 took over stock of ₹10,000 at 10% discount and the balance was paid to them in cash.

(*d*) There was an old typewriter which had been written off completely. It was estimated to realize ₹600. It was taken away by Rajat at 25% less than the estimated price.

(*e*) Aman agreed to take over the responsibility of completing dissolution at an agreed remuneration of ₹1,000 and to bear all realization expenses. Actual realisation expenses ₹800 were paid by the firm.

(*f*) Loss on realization was ₹54,000. *(C.B.S.E. 2017, Comptt. Delhi)*

[**Ans.** (*a*) (*b*) & (*c*) : Debit Realisation A/c and Credit Bank A/c.

(*d*) Debit Rajat's Capital A/c and Credit Realisation A/c.

(*e*) Debit Realisation A/c by ₹1,000; Credit Bank A/c by ₹800 and Aman's Capital A/c by ₹200.

(*f*) Debit Aman's Capital A/c by ₹36,000 and Rajat's Capital A/c by ₹18,000; Credit Realisation A/c by ₹54,000.]

Q. 34. Disha, Mohit and Nandan are partners. They decide to dissolve their firm. Pass necessary Journal Entries for the following after various Assets (other than Cash and Bank) and the third party liabilities have been transferred to Realisation Account :

(*a*) An old typewriter which was not recorded in the books was sold for ₹2,000 whereas its expected value was ₹5,000.

(*b*) Stock of ₹70,000 was taken by Disha at a discount of 30%.

(*c*) Total creditors of the firm were ₹20,000. A creditor for ₹2,000 was untraceable and other creditors accepted payment allowing 10% discount.

(*d*) Mohit paid realisation expenses of ₹18,000 out of his private funds, who was to get remuneration of ₹13,000 for completing the dissolution process and was responsible to bear all the realisation expenses.

(*e*) Nandan had taken a loan of ₹50,000 from the firm, which was paid fully by him to the firm.

(*f*) ₹12,000 was recovered from a debtor which was written off as Bad debts last year.

[**Ans.** (*a*) Debit Bank A/c and Credit Realisation A/c by ₹2,000.

(*b*) Debit Disha's Capital A/c and Credit Realisation A/c by ₹49,000.
(*c*) Debit Realisation A/c and Credit Bank A/c by ₹16,200.
(*d*) Debit Realisation A/c and Credit Mohit's Capital A/c by ₹13,000.
(*e*) Debit Bank A/c and Credit Nandan's Loan A/c by ₹50,000.
(*f*) Debit Bank A/c and Credit Realisation A/c by ₹12,000.]

Q. 35. Angad, Raman and Harshit were partners in a firm. They decided to dissolve their firm. Pass necessary journal entries for the following after various assets (other than cash and bank) and the third party liabilities have been transferred to Realisation Account :

(*i*) There was a stock of ₹90,000. Raman took over 50% of the stock at 10% discount and remaining stock was sold at 40% profit on book value.

(*ii*) Profit and Loss A/c was showing a debit balance of ₹15,000 which was distributed among the partners.

(*iii*) A machinery which was not recorded in the books was sold for ₹2,000.

(*iv*) Angad was paid only ₹5,000 (in full settlement) for his loan to the firm which amounted to ₹5,500.

(*v*) Realisation expenses amounting to ₹5,000 paid by Harshit.

(*vi*) There were 100 shares of ₹10 each in DCM Ltd. acquired at a cost of ₹1,200 which had been written off completely from the books. These shares are valued at ₹9 each and divided among the partners in their profit sharing ratio.

[**Ans.** (*i*) Debit Raman's Capital A/c by ₹40,500 and Bank A/c by ₹63,000 and Credit Realisation A/c by ₹1,03,500.

(*ii*) Debit Partner's Capital A/cs by ₹5,000 each and credit Profit & Loss Account by ₹15,000.

(*iii*) Debit Bank A/c and Credit Realisation A/c by ₹2,000.

(*iv*) Debit Angad's Loan A/c by ₹5,500 and Credit Bank A/c by ₹5,000 and Realisation A/c by ₹500.

(*v*) Debit Realisation A/c and Credit Harshit's Capital A/c by ₹5,000.

(*vi*) Debit Partner's Capital A/cs by ₹300 each and Credit Realisation A/c by ₹900.]

Q. 36. *X* and *Y* are partners. They decided to dissolve their firm. Pass necessary entries assuming that various assets and external liabilities have been transferred to Realisation Account :

(1) *X*'s loan was appearing on the liabilities side of Balance Sheet at ₹40,000. He accepted an unrecorded asset of ₹60,000 in full settlement of his account.

(2) There was an unrecorded asset estimated at ₹20,000, half of which was handed over to an unrecorded liability of ₹30,000 in settlement of a claim of ₹18,000 and remaining half was sold in the market at 80% of its value.

(3) Raman, a Creditor to whom ₹25,000 were due to be paid, accepted an unrecorded computer of ₹18,000 at a discount of 10% and the balance was paid to him in Cash.

(4) Sudhir, an unrecorded creditor of ₹40,000 accepted an unrecorded vehicle of ₹20,000 at ₹25,000 and the balance was paid to him in Cash.

(5) There was a Contingent liability in respect of bill discounted but not matured ₹20,000.

(6) Furniture of ₹20,000 and goodwill of ₹30,000 were appearing in the Balance Sheet but no other information was provided regarding these two items.

[**Ans.**

(1) Debit *X*'s Loan A/c and Credit Realisation A/c by ₹40,000.

(2) (*i*) Debit Realisation A/c and Credit Bank A/c by ₹12,000

(*ii*) Debit Bank A/c and Credit Realisation A/c by ₹8,000

(3) Debit Realisation A/c and Credit Bank A/c by ₹8,800

(4) Debit Realisation A/c and Credit Bank A/c by ₹15,000

(5) No entry

(6) No entry]

ADDITIONAL QUESTIONS (FOR PRACTICE)

Q. 37. Harish and Gopal were partners in a firm sharing profits in the ratio of 3 : 2. On 31st March, 2018, their Balance Sheet was as follows :

BALANCE SHEET OF HARISH AND GOPAL

as at March 31, 2018

Liabilities		*Amount*	*Assets*	*Amount*
		₹		₹
Creditors		36,000	Cash	47,000
Outstanding Expenses		10,000	Bank	93,000
Gopal's Wife's Loan		50,000	Debtors	76,000
Capitals :			Stock	2,00,000
Harish	2,80,000		Furniture	20,000
Gopal	1,60,000	4,40,000	Leasehold Premises	1,00,000
		5,36,000		5,36,000

On the above date the firm was dissolved. Various assets were realized and liabilities were settled as under :

(*i*) Gopal agreed to pay his wife's loan.

(*ii*) Leasehold premises realised ₹1,50,000 and Debtors ₹12,000 less.

(*iii*) Half of the creditors agreed to accept furniture of the firm as full settlement of their claim and remaining half agreed to accept 10% less.

(*iv*) 50% stock was taken over by Harish on payment by cheque of ₹90,000 and remaining stock was sold for ₹94,000.

(*v*) Realization expenses of ₹10,000 were paid by Gopal on behalf of the firm.

Prepare Realization Account. *(C.B.S.E. 2020, Punjab)*

[**Ans.** Profit on Realisation ₹11,800.]

Q. 38. Michael, Jackson and John were partners in a firm sharing profits in the ratio of 3 : 1 : 1. On 31st March, 2017, they decided to dissolve their firm. On that date their Balance Sheet was as follows :

Balance Sheet of Michael, Jackson and John as at 31.3.2017

Liabilities		*Amount*	*Assets*		*Amount*
		₹			₹
Creditors		11,500	Bank		6,000
Loan		3,500	Debtors	48,400	
Capitals :			*Less* : Provision for		
Michael	50,000		Doubtful Debts	2,400	46,000
Jackson	25,000		Stock in Trade		16,000
John	14,000	89,000	Furniture		2,000
			Sundry Assets		34,000
		1,04,000			1,04,000

It was agreed that :

(*i*) Michael was to take over Furniture at ₹2,600 and Debtors amounting to ₹40,000 at ₹34,400 and the Creditors of ₹10,000 were to be paid by him at this figure.

(*ii*) Jackson was to take over all the stock in trade at ₹14,000 and some of the other Sundry Assets at ₹28,800 (being 10% less than book value).

(*iii*) John was to take over the remaining Sundry Assets at 90% of the book value and assumed the responsibility for the discharge of the loan.

(*iv*) The remaining debtors were sold to a debt collecting agency for 50% of the book value. The expenses of dissolution ₹600 were paid by John.

Prepare Realisation Account, Bank Account and Partners' Capital Accounts.

(C.B.S.E. 2019, Delhi)

[**Ans.** Loss on Realisation ₹12,800; Final payment to Michael ₹15,320 and to John ₹13,740; Amount brought in by Jackson ₹20,360; Total of Bank A/c ₹30,560.]

Q. 39. Srijan, Raman and Manan were partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1. On 31st March, 2017 their Balance Sheet was as follows :

Balance Sheet of Srijan, Raman and Manan as at 31-3-2017

Liabilities		₹	*Assets*	₹
Capitals :			Capital : Manan	10,000
Srijan	2,00,000		Plant	2,20,000
Raman	1,50,000	3,50,000	Investments	70,000
Creditors		75,000	Stock	50,000
Bills Payable		40,000	Debtors	60,000
Outstanding Salary		35,000	Bank	10,000
			Profit and Loss Account	80,000
		5,00,000		5,00,000

On the above date they decided to dissolve the firm.

(i) Srijan was appointed to realise the assets and discharge the liabilities. Srijan was to receive 5% commission on sale of assets (except cash) and was to bear all expenses of realisation.

(ii) Assets were realised as follows :

	(₹)
Plant	85,000
Stock	33,000
Debtors	47,000

(iii) Investments were realised at 95% of the book value.

(iv) The firm had to pay ₹7,500 for an outstanding repair bill not provided for earlier.

(v) A contingent liability in respect of bills receivable, discounted with the bank had also materialised and had to be discharged for ₹15,000.

(vi) Expenses of realisation amounting to ₹3,000 were paid by Srijan.

Prepare Realisation Account, Partners' Capital Accounts and Bank Account. *(C.B.S.E. 2018)*

[Ans. Loss on Realisation ₹2,02,575; Cash brought in by Mohan 66,515; Final Payment to Srijan ₹98,545 and Raman ₹36,970; Total of Bank Account ₹3,08,015.]

Q. 40. *A, B* and *C* are partners sharing profits and losses in the ratio of 3 : 2 : 1. On 31st March, 2022, their Balance Sheet was as follows :

Liabilities		₹	*Assets*		₹
Creditors		46,200	Cash at Bank		10,500
Bills Payable		10,800	Stock		59,400
A's Loan		57,000	Debtors	57,000	
Capitals :			*Less* : Provision	3,000	54,000
A	60,000		Plant and Machinery		1,31,100
B	12,000				
C	60,000	1,32,000			
Reserve Fund		9,000			
		2,55,000			2,55,000

The firm was dissolved on 1st April, 2022.

There was an unrecorded asset of ₹60,000. It was sold for ₹15,000. The assets were realised as under : Stock ₹45,000; Goodwill ₹12,000; Debtors 60% of the book value; Machinery ₹90,000; Liabilities were paid in full. In addition, a bill for ₹6,000 under discount was dishonoured and had to be taken up by the firm.

The expenses on realisation amounted to ₹2,400.

You are required to prepare the Realisation A/c, Partner's Capital Accounts, and Bank A/c.

[Ans. Loss on Realisation ₹56,700; Final Payments to *A* ₹36,150; and to *C* ₹52,050; Cash brought in by *B* ₹3,900; Total of Bank A/c ₹2,10,600]

Hint : There will be no entry for ₹60,000 in respect of unrecorded asset. For this, only ₹15,000 will be credited to Realisation A/c and debited to Bank A/c.

Q. 41. *A, B* and *C* are in partnership sharing profits and losses in the proportions of 1/2, 1/3 and 1/6 respectively. On 31st January, 2022 they decide to dissolve the partnership, and the position of the firm on this date is represented by the following Balance Sheet :

Liabilities	₹	*Assets*	₹
Creditors	40,000	Land and Buildings	57,000
Loan Account : *A*	10,000	Stock	50,000
Capital Accounts :		Sundry Debtors	50,000
A	60,000	Cash at Bank	3,000
B	40,000		
C	10,000		
	1,60,000		1,60,000

During the course of realisation, a liability under a suit for damages is settled at ₹20,000 as against ₹5,000 only provided for in the books of the firm.

Land and Buildings were sold for ₹40,000 and the Stock and Sundry Debtors realised ₹30,000 and ₹42,000 respectively. The expenses of realisation amounted to ₹1,200. You are required to prepare Realisation Account, Cash Account and Partners' Capital Accounts in the books of the firm.

[**Ans.** Loss on Realisation ₹61,200; Cash paid to *A* ₹29,400; *B* ₹19,600 and Cash brought in by C ₹200; Total of Bank A/c ₹1,15,200]

Hints. : 1. Amount paid for damages ₹20,000. Realisation A/c will be debited and Bank A/c will be credited from this amount.

2. Liability for damages ₹5,000 is already included in the Creditors appearing in the Balance Sheet. As such, Creditors will be paid ₹35,000 net.

Q. 42. The following is the Balance Sheet of *X* and *Y* as at 30th June, 2022.

Liabilities	₹	*Assets*		₹
Sundry Creditors	20,000	Goodwill		10,000
Bills Payable	20,000	Buildings		25,000
Bank Overdraft	8,000	Plant		25,000
Outstanding Expenses	2,000	Investments		15,300
X's brother's Loan	20,000	Stock		8,700
Y's Loan	10,000	Debtors	17,000	
Investment Fluctuation Fund	2,800	*Less* : Provision	2,000	15,000
Employees' Provident Fund	1,200	Bills Receivable		10,000
General Reserve	2,000	Cash & Bank		13,000
X's Capital	20,000	Profit and Loss A/c (Dr. Balance)		4,000
Y's Capital	20,000			
	1,26,000			1,26,000

The firm was dissolved on 30th June, 2022 and the following arrangements were decided upon :

(*a*) *X* agreed to pay off his brother's loan;

(*b*) Debtors realised ₹12,000;

(c) *Y* took over all the investments at ₹12,000.

(d) Other assets realised as follows :
Plant — ₹20,000, Building — ₹50,000, Goodwill — ₹6,000

(e) Sundry Creditors and bills payable were settled at 5% discount, *Y* accepted Stock at ₹8,000 and *X* took over Bills Receivable at 20% discount.

(f) Realisation Expenses amounted to ₹2,000.

You are required to pass Journal Entries.

[**Ans.** Profit on Realisation ₹9,800; Final Payment to *X* ₹35,900 and *Y* ₹3,900; Total of Bank A/c ₹1,01,000.]

Q. 43. *A* and *B* were partners from 1.4.2020 with capitals of ₹60,000 and ₹40,000 respectively. They shared profits and loses in the ratio of 3 : 2. They carried on business for two years. In the first year ending on 31.3.2021 they made a profit of ₹50,000 but in the second year ending on 31.3.2022, a loss of ₹20,000 was incurred. As the business was no longer profitable they dissolved the firm on 31.3.2022. Creditors on that date were ₹20,000. The partners withdrew for personal use ₹8,000 per partner per year. The assets realised ₹1,00,000. The expenses of realisation were ₹3,000.

Prepare Realisation Account, Partners' Capital Accounts and Bank Account.

[**Ans.** Balances of Capital A/cs before Dissolution *A* ₹62,000 and *B* ₹36,000; Total Assets ₹1,18,000; Loss on Realisation ₹21,000; Final Payments *A* ₹49,400; and *B* ₹27,600; Total of Bank A/c ₹1,00,000]

Q. 44. *A* and *B* have been in business together for the last three years ending 31st March, 2022 at which date they agree to dissolve. Their capital at the commencement of the business was ₹30,000 and ₹20,000 respectively. Profits and Losses were shared in the ratio of 3 : 2. The results of the three years before allowing 10% p.a. interest on capital were : 31-3-2020 profit ₹30,000, 31-3-2021 profit ₹22,200 and 31-3-2022 loss ₹5,380. Drawings of each partner is ₹4,000 per year. Creditors on the date of dissolution were ₹16,400. The assets realised ₹85,000. Expenses of dissolution amounted to ₹780.

Prepare (*i*) Profit and Loss Appropriation Account; (*ii*) Capital Accounts before and after dissolution; (*iii*) Memorandum Balance Sheet; (*iv*) Bank A/c; (*v*) Realisation Account.

[**Ans.** Balances of Capital Accounts before dissolution *A* ₹46,172 and *B* ₹26,648; Loss on Realisation ₹5,000; Cash paid to *A* ₹43,172 and *B* ₹24,648.]

Q. 45. The following was the Balance Sheet of Fox and Wolf as at 31st March 2018, when they decided to dissolve the firm :

Liabilities		₹	*Assets*	₹
Capital :			Cash at Bank	4,500
Fox	30,000		Stock	18,000
Wolf	24,000	54,000	Debtors	42,000
Creditors		88,500	Furniture	12,000

Mrs. Wolf's Loan	40,000	Machinery	1,06,500
Bills Payable	23,000	Profit & Loss A/c	22,500
	2,05,500		2,05,500

The assets realised :

Stock	₹10,500
Debtors	₹27,750
Machinery	₹88,500

Furniture was taken over by Fox at ₹7,500. Bills payable were paid in full, while creditors were settled at 2% discount. Mrs. Wolf accepted ₹38,500 in full settlement of her Loan Account.

There was a claim of damages against the firm for ₹4,000 which was settled at ₹2,000.

One customer, whose account was written off as bad, now paid ₹1,800, which is not included in ₹27,750 given above. Actual realisation expenses amounted to ₹2,100.

Prepare (*a*) Realisation A/c, (*b*) Capital Accounts of Partners, (*c*) Bank Account to close the Books of the firm.

[**Ans.** Loss on Realisation ₹43,280; Amount brought in by Fox ₹10,390 and Wolf ₹8,890; Total of Bank Account ₹1,52,330.]

Q. 46. Bale and Yale are equal partners of a firm, the Balance Sheet of which is given below as at 31.3.2022, the date on which they decide to dissolve the firm.

BALANCE SHEET *as at 31.3.2022*

Liabilities		₹	*Assets*	₹
Capital Accounts :			Building	45,000
Bale	50,000		Machinery	15,000
Yale	40,000	90,000	Furniture	12,000
General Reserve		8,000	Debtors	8,000
Bale's Loan		3,000	Stock	24,000
Creditors		14,000	Bank	11,000
		1,15,000		1,15,000

(*i*) The assets realised were as follows :
Stock ₹22,000; Debtors ₹7,500; Machinery ₹16,000; Building ₹35,000.

(*ii*) Bale agreed to accept ₹2,500 in full settlement of his loan account.

(*iii*) Yale took over the furniture at ₹9,000.

(*iv*) Dissolution expenses amounted to ₹2,500.

Prepare (*a*) Realisation Account; (*b*) Capital Accounts of Partners; (*c*) Bale's Loan Account; (*d*) Bank Account.

[**Ans.** Loss on Realisation ₹16,500; Final Payment to Bale ₹45,750 and Yale ₹26,750. Total of Bank Account ₹91,500.]

Hint : Entry for payment of Bale's Loan will be :

Bale's Loan A/c	Dr.	3,000	
To Bank A/c			2,500
To Realisation A/c			500

Q. 47. Sanjay and Sameer were partners in a firm sharing profits in the ratio of 2 : 3. On 31.3.2018 their Balance Sheet was as follows :

BALANCE SHEET OF SANJAY AND SAMEER

as at 31.3.2018

Liabilities		₹	*Assets*	₹
Capitals :			Land and Building	3,00,000
Sanjay	2,00,000		Stock	1,00,000
Sameer	3,00,000	5,00,000	Debtors	1,50,000
Creditors		1,05,000	Bank	1,55,000
Workmen Compensation Reserve		1,00,000		
		7,05,000		7,05,000

The firm was dissolved on 1.4.2018 and the assets and liabilities were settled as follows :

(*i*) Sanjay agreed to take over land and building at ₹3,50,000 by paying cash;

(*ii*) Stock was sold for ₹90,000;

(*iii*) Creditors accepted Debtors in full settlement of their claim.

Pass necessary journal entries for dissolution of the firm.

[**Ans.** Final payment to Sanjay ₹2,38,000 and Sameer ₹3,57,000.]

Hints : (*i*) Prepare Realisation A/c in working notes. Loss on Realisation will be ₹5,000.
(*ii*) Workmen Compensation Reserve will be credited to Partner's Capital Accounts.
(*iii*) There will be no entry for Creditors taking over Debtors in full settlement

Q. 48. Arun, Tarun and Varun shared profits in the ratio of 2 : 2 : 1. On 31.12.2021 their Balance Sheet was as follows :

Liabilities		₹	*Assets*	₹
Creditors		50,000	Cash	30,000
Bills Payable		30,000	Debtors	50,000
Provident Fund		20,000	Stock	36,000
Investment Fluctuation Fund		8,000	Investments	20,000
Commission Received in Advance		12,000	Plant	90,000
Capitals :			Profit & Loss A/c	34,000
Arun	50,000			
Tarun	60,000			
Varun	30,000	1,40,000		
		2,60,000		2,60,000

On this date the firm was dissolved. Arun was appointed to realise the assets. Arun was to receive 5% commission on the sale of assets (except cash) and was to bear all expenses of realisation.

Arun realised the assets as follows :

Stock ₹36,000, Debtors ₹45,000, Investments 80% of the book value, Plant ₹65,500. Expenses of realisation amounted to ₹5,500. Commission received in advance was returned to the customers after deducting ₹4,000. Firm had to pay ₹8,000 for outstanding wages. This liability was not provided for in the above Balance Sheet. ₹20,000 had to be paid for provident fund.

Prepare Realisation Account, Capital Accounts and Cash Account.

[**Ans.** Loss on Realisation ₹37,625; Final Payment Arun ₹29,475, Tarun ₹31,350 and Varun ₹15,675; Total of Cash A/c ₹1,92,500.]

Hint. There will be no entry for the expenses of realisation, as these will be met by Arun personally.

Q. 49. Arnab, Ragini and Dhrupad were partners sharing profits in the ratio of 3 : 1 : 1. On 31st March, 2015, they decided to dissolve their firm. On that date their Balance Sheet was as under :

BALANCE SHEET OF ARNAB, RAGINI AND DHRUPAD

as at 31st March, 2015

Liabilities			₹	*Assets*		₹
Creditors			60,000	Bank		50,000
Arnab's Brother's Loan			95,000	Debtors	1,70,000	
Dhrupad's Loan			1,00,000	*Less* : Provision for		
Investment Fluctuation Fund			50,000	Bad Debts	20,000	1,50,000
Capitals :	Arnab	2,75,000		Stock		1,50,000
	Ragini	2,00,000		Investments		2,50,000
	Dhrupad	1,70,000	6,45,000	Building		3,00,000
				Profit and Loss Account		50,000
			9,50,000			9,50,000

The assets were realised and the liabilities were paid as under :

(*i*) Arnab agreed to pay his brother's loan.

(*ii*) Investments realised 20% less.

(*iii*) Creditors were paid at 10% less.

(*iv*) Building was auctioned for ₹3,55,000. Commission on auction was ₹5,000.

(*v*) 50% of the stock was taken over by Ragini at market price which was 20% less than the book value and the remaining was sold at market price.

(*vi*) Dissolution expenses were ₹8,000. ₹3,000 were to be borne by the firm and the balance by Dhrupad. The expenses were paid by him.

Prepare Realisation Account, Bank Account and Partner's Capital Accounts.

[**Ans.** Loss on Realisation ₹1,27,000; Final Payment : Arnab ₹2,63,800; Ragini ₹1,04,600 and Dhrupad ₹1,37,600; Total of Bank A/c ₹6,60,000.]

Hint. Realisation of Building will be recorded at the net amount of ₹3,50,000.

Q. 50. *A, B* and *C* sharing profits and losses in the ratio of 3 : 2 : 1 agreed to dissolve their partnership firm on 31st March, 2022. *A* was asked to realise the assets and pay off liabilities. He had to bear the realisation expenses for which he was promised a lump sum amount of ₹3,000. Their financial position as at that date was as follows :

Liabilities		₹	*Assets*	₹
Accounts Payable		40,000	Goodwill	20,000
Mortgage Loan		30,000	Lease	75,000
Advance from *B*		25,000	Patents	6,000
Employees' Saving Bank		16,000	Stock	50,000
Capitals :			Accounts Receivable	25,000
A	80,000		Equipment	20,000
B	66,000	1,46,000	300 Shares in *X* Ltd.	36,000
			Cash	13,000
			C's Capital	12,000
		2,57,000		2,57,000

Informations :

(1) Stock was valued at ₹40,000 and this was taken over by *A* and *B* equally. Lease realised ₹1,10,000; Equipments at ₹18,000; and Accounts Receivable at ₹20,000 and other assets proved valueless.

(2) Actual realisation expenses paid by *A* amounted to ₹1,800.

(3) There was an unrecorded asset of ₹10,000 which was taken over by *A* at ₹12,000.

(4) A bill of ₹3,200 due for sales tax was received during the course of realisation and this was also paid.

(5) Sunil, an old customer whose account was written off as bad in the previous year, paid ₹2,500 which is not included in the above stated accounts receivable.

(6) Market value of the Shares in *X* Ltd. is ₹100 per share. Half the shares were sold in the market subject to a commission of 2% and the balance half were divided by all the partners in their profit sharing ratio.

Prepare necessary accounts.

[**Ans.** Loss on Realisation ₹6,000; Cash brought in by *C* ₹15,500; Payment to *A* ₹40,500 and *B* ₹39,000; Total of Cash A/c ₹1,93,700.]

Hints : **(1)** Cash realised from sale of shares :

		₹
150 Shares @ ₹100 each	=	15,000
Less : 2% of 15,000	=	300
		14,700

(2) No entry need to be passed for realisation expenses of ₹1,800 paid by *A*. Only the following entry may be passed for ₹3,000 promised to be paid to *A* :

Realisation A/c	Dr.	3,000	
To *A*			3,000

(3) Accounts Payable, Mortgage Loan, Advance from *B* and Employees' Saving Bank will be paid in full.

Q. 51. *X*, *Y* and *Z* decided to dissolve their partnership firm. The position as at 31st December, 2021, the date of dissolution was as follows :

Liabilities		₹	*Assets*	₹
Creditors		20,000	Freehold Property	40,000
Bank Loan		5,000	Machinery	40,000
Capitals : *X*	70,000		Investments	16,000
Y	40,000		Stock	30,000
Z	20,000	1,30,000	Debtors	30,000
Current Accounts :			Cash	10,000
X	12,000		Loss in Business	20,000
Y	7,500	19,500	Current Account :	
Reserve for Contingency		10,000	*Z*	4,500
Commission Received in Advance		6,000		
		1,90,500		1,90,500

They shared profits in the ratio of *X* : 1/2, *Y*: 3/10 and *Z* : 1/5.

X agreed to bear all realisation expenses. For this service *X* is paid ₹2,000. Actual expenses amounted to ₹3,200 which was withdrawn by him from the firm.

Other informations are :

(1) Assets, with the exception of investments and Cash, are sold for ₹1,25,100. 75% of the investments are taken over by *X* at 75% of their book value. He also agrees to discharge the Bank Loan. The remaining investments were taken over by *Y* at the market value of 120%.

(2) There were outstanding expenses amounting to ₹5,000. These were settled for ₹2,000.

(3) A B/R for ₹10,000 was received from a customer Mr. Surender Kumar and the bill was discounted from the bank. Surender became insolvent and 75 paise per rupee were received from his estate.

(4) Commission received in advance was returned to the Customers after deducting 60% for work done.

You are required to prepare the necessary accounts.

[**Ans.** Loss on Realisation ₹20,000; Final Payment to *X* ₹61,800; *Y* ₹33,700 and *Z* ₹9,500; Total of Cash A/c ₹1,42,600.]

Hints : 1. Reserve for contingency will be credited to Capital Accounts

2. Following entries will be passed for realisation expenses :

		Dr. (₹)	Cr. (₹)
(*i*) Realisation A/c	Dr.	2,000	
To *X*			2,000
(*ii*) *X*	Dr.	3,200	
To Cash			3,200

3. Following entry may be passed on account of B/R discounted :

		Dr. (₹)	Cr. (₹)
(*i*) Cash	Dr.	7,500	
To Realisation A/c			7,500
(*ii*) Realisation A/c	Dr.	10,000	
To Cash			10,000

Q. 52. *A* and *B* shared profits in the ratio of 7 : 3. They dissolved the firm and appointed *A* to realise the assets. *A* is to receive 6% commission on the amount realised from Stock, Debtors, B/R and Shares.

The position of the firm was as follows :

Liabilities	₹	*Assets*	₹
Creditors	60,000	Plant and Machinery	20,000
Repairs and Renewals Reserve	4,000	Prepaid Insurance	1,200
Bank Loan	20,000	Stock	60,000
A's Capital A/c	50,000	100 Shares in D.C.M. Ltd.	5,000
B's Capital A/c	20,000	Sundry Debtors	38,000
		B/R	6,000
		Cash at Bank	8,800
		A's Current A/c	5,000
		Profit & Loss Account	10,000
	1,54,000		1,54,000

Informations :

1. *A* realised the assets as follows :— Full amount from Sundry Debtors and B/R except from one for ₹2,000 being insolvent. Stock realised ₹52,000; Shares in D.C.M. were sold for ₹60 each.
2. Half the trade creditors accepted plant and machinery at an agreed valuation of 10% less than the book value and cash of ₹7,000 in full settlement of their claims.
3. Remaining creditors were paid off at a discount of 10%. Expenses of realisation amounted to ₹700.
4. One quarter's tax amounting to ₹1,500 was due and had to be paid.
5. There was a contingent liability amounting to ₹13,000. It was settled for ₹6,000.
6. Bank Loan was discharged along with interest due for two months @ 18% p.a.

Prepare necessary accounts.

[**Ans.** Loss on Realisation ₹19,000; Amount paid to *A* ₹33,500 and to *B* ₹12,500; Total of Bank A/c ₹1,08,800.]

Hints : (1) Creditors for ₹30,000 accept Plant and Machinery at ₹18,000 and Cash ₹7,000. The balance of ₹5,000 will be treated as discount. Remaining Creditors of ₹30,000 are paid ₹27,000 in full settlement. Hence, the total Cash paid to Creditors = ₹7,000 + ₹27,000 = ₹34,000

(2) Commission paid to *A* (For sale of assets) 6% on ₹1,00,000 = ₹6,000.

(3) Repairs and Renewals Reserve will be transferred to the Credit side of Capital A/cs.

Q. 53. *A*, *B* and *C* are equal partners in a firm. The Balance Sheet of the firm at the date of dissolution was as follows :

Liabilities	₹	*Assets*	₹
Creditors	40,000	Lease	80,000
Provision for Depreciation on Plant	8,600	Plant	40,000

A's Wife Loan		10,000	Patent Rights		30,000
Capital Accounts :			Furniture		15,000
A	62,000		Stock		20,000
B	54,000		Book Debts	26,000	
C	51,000		*Less* : Provision	1,000	25,000
		1,67,000	Cash at Bank		14,000
			Cash-in-Hand		1,600
		2,25,600			2,25,600

B was appointed to realise the assets and pay the liabilities. He was entitled to receive 10% commission on the amounts finally paid to other partners as capital. He was also to bear the expenses of realisation.

You are informed that :

(1) An old typewriter, written off completely from the firm's books, is now estimated to realise ₹1,400. It is taken over by *B* at this estimated price.

(2) *A* agreed to accept furniture in full settlement of his wife's loan.

(3) Assets realised as follows : Lease ₹1,00,000; Plant at ₹36,000; Stock ₹12,000; ₹8,000 of the book debts proved bad.

(4) Expenses of realisation amounted to ₹800.

(5) Creditors accepted patent rights at a discount of 20% in part satisfaction of their claim. Out of their balance they were paid 50% in full satisfaction.

(6) The partnership had previously purchased some shares at ₹20,000 in a public limited company and had written them off as worthless. These shares were taken over by *B* at ₹4,000.

Prepare necessary accounts.

[**Ans.** Profit on Realisation ₹12,000; Final Payment *A* ₹60,000; *B* ₹63,600 and *C* ₹50,000; Total of Bank A/c ₹1,81,600.]

Hints : (1) Commission Payable to *B* will be : ₹

10/110 on payment to *A* $= 66{,}000 \times \frac{10}{110} = 6{,}000$

10/110 on payment to *C* $= 55{,}000 \times \frac{10}{110} = 5{,}000$

11,000

(2) There will be no entry for the payment of realisation expenses and *A*'s Wife Loan. Creditors will be paid only ₹8,000.

(3) Provision for Depreciation on Plant will be Credited to Realisation A/c and no further entry will be passed for it.

Q. 54. Susan, Geeta and Rashi are partners sharing profits and losses in the ratio of 5 : 3 : 2. Their Balance Sheet as at 31st March, 2017, is as under :

BALANCE SHEET OF SUSAN, GEETA AND RASHI

as at 31st March, 2017

Liabilities	*Amount*	*Assets*	*Amount*
	₹		₹
Sundry Creditors	50,000	Cash at Bank	70,000

Workmen Compensation Reserve		25,000	Sundry Debtors	65,000	
Employees Providend Fund		5,000	*Less* : Provision for		
Bank Loan		55,000	Doubtful Debts	(5,000)	60,000
Capital A/cs			Goodwill		50,000
Susan	2,20,000		Furniture		1,00,000
Geeta	1,70,000		Building		3,80,000
Rashi	1,35,000	5,25,000			
		6,60,000			6,60,000

The partners decided to dissolve their partnership on 31st March, 2017.

The following transactions took place at the time of dissolution :

(*a*) Realization expenses of ₹2,000 were paid by Susan on behalf of the firm.

(*b*) Geeta took over the goodwill for her own business at ₹40,000.

(*c*) Building was taken over by Rashi at ₹3,00,000.

(*d*) Only 80% of the debtors paid their dues.

(*e*) Furniture was sold for ₹97,000.

(*f*) Bank Loan was settled along with interest of ₹5,000.

You are required to prepare the Realization Account. (*I.S.C. 2018*)

[**Ans.** Loss on Realisation ₹1,08,000.]

Q. 55. *P* and *Q* share profits and losses in 5 : 3. What Journal entries would be passed for the following transactions on the dissolution of their firm, after various assets (other than cash) and third party liabilities have been transferred to Realisation Account?

(*i*) Profit and Loss Account (Dr. Balance) appeared in the books at ₹30,000.

(*ii*) *P* was asked to look into the dissolution of the firm for which he was allowed a commission of ₹2,500.

(*iii*) *Q* took over part of the stock at ₹6,400 (being 20% less than the book value).

(*iv*) An unrecorded liability amounting to ₹10,000 was settled at ₹8,000.

(*v*) Motor Car of the book value of ₹80,000 taken over by Creditors of the book value of ₹60,000 in full settlement.

[**Ans.** (*i*) Debit Partner's Capital A/cs in profit sharing ratio and Credit Profit & Loss A/c.
(*ii*) Debit Realisation A/c and Credit *P*'s Capital A/c.
(*iii*) Debit *Q*'s Capital A/c and Credit Realisation A/c by ₹6,400.
(*iv*) Debit Realisation A/c and Credit Bank A/c by ₹8,000.
(*v*) No entry for asset taken over by Creditors.]

Q. 56. Ravi and Mukesh were partners in a firm sharing profit and losses equally. On 31st March, 2019 their firm was dissolved. On the date of dissolution their Balance Sheet showed stock of ₹60,000 and creditors of ₹70,000. After transferring stock and creditors to realisation account the following transactions took place :

(*i*) Ravi took over 40% of total stock at 20% discount.

(ii) 30% of total stock was taken over by creditors of ₹20,000 in full settlement.

(iii) Remaining stock was sold for cash at a profit of 25%.

(iv) Remaining creditors were paid in cash at a discount of 10%.

Pass necessary journal entries for the above transactions in the books of the firm.

(C.B.S.E. 2019, Comptt)

[**Ans.** (i) Debit Ravi's Capital A/c and Credit Realisation A/c by ₹19,200.

(ii) No Entry.

(iii) Debit Cash A/c and Credit Realisation A/c by ₹22,500.

(iv) Debit Realisation A/c and Credit Cash A/c by ₹45,000.]

Q. 57. Pass the necessary journal entries for the following transactions on the dissolution of the partnership firm of Tony and Rony after the various assets (other than cash) and external liabilities have been transferred to Realization Account :

(i) An unrecorded asset of ₹2,000 and cash ₹3,000 was paid for liability of ₹6,000 in full settlement.

(ii) 100 shares of ₹10 each have been taken over by partners at market value of ₹20 per share in their profit sharing ratio, which is 3 : 2.

(iii) Stock of ₹30,000 was taken over by a creditor of ₹40,000 at a discount of 30% in full settlement.

(iv) Expenses of realisation ₹4,000 were to be borne by Rony. Rony used the firm's cash for paying these expenses.

(C.B.S.E. 2020, Chennai, Mumbai)

Ans. (i) Debit Realisation A/c and Credit Cash by ₹3,000.

(ii) Debit Tony's Capital A/c by ₹1,200 and Rony's Capital A/c by ₹800 and Credit Realisation A/c by ₹2,000.

(iii) No Entry.

(iv) Debit Rony's Capital A/c and Credit Cash A/c by ₹4,000.

Q. 58. Raina and Meena were partners in a firm sharing profits and losses equally. They dissolved their firm on 31st March, 2018.

On this date, the Balance Sheet of the firm, apart from realizable assets and outside liabilities showed the following :

	₹	
Raina's Capital	40,000	(Cr.)
Meena's Capital	20,000	(Dr.)
Profit and Loss Account	10,000	(Dr.)
Raina's Loan to the Firm	15,000	
Contingency Reserve	7,000	

On the date of dissolution of the firm :

(a) Raina's loan was repaid by the firm along with interest of ₹500.

(b) The dissolution expenses of ₹1,000 were paid by the firm on behalf of Raina who had to bear these expenses.

(c) An unrecorded asset of ₹2,000 was taken over by Meena while Raina discharged an unrecorded liability of ₹3,000.

(d) The dissolution resulted in a loss of ₹60,000 from the realization of assets and settlement of liabilities.

You are required to prepare :

(i) Partner's Capital Accounts.

(ii) Raina's Loan Account. (I.S.C. 2019)

SOLUTION :

Dr. Partners' Capital Accounts Cr.

Liabilities	*Raina*	*Meena*	*Particulars*	*Raina*	*Meena*
	₹	₹		₹	₹
To Bal. b/d		20,000	By Bal. b/d	40,000	
To Realisation A/c		2,000	By Realisation A/c	3,000	
To Profit & Loss A/c	5,000	5,000	By Contingency Reserve A/c	3,500	3,500
To Realisation A/c (loss)	30,000	30,000	By Bank A/c (Deficit brought in)		53,500
To Bank A/c (exp)	1,000				
To Bank A/c	10,500				
	46,500	57,000		46,500	57,000

Dr. Raina's Loan Account Cr.

Particulars	*Amount*	*Particulars*	*Amount*
	₹		₹
To Bank A/c	15,500	By Balance b/d	15,000
		By Realisation A/c	500
	15,500		15,500

Q. 59. Mike and Ajay are partners sharing profits and losses in proportion to their capitals, which on 31st March, 2019, stood at ₹6,00,000 and ₹4,00,000 respectively. On this date, the firm had ₹1,00,000 in its Workmen Compensation Reserve and its outside liabilities amounted to ₹6,00,000, which included Creditors of ₹2,00,000 and Bills Payable of ₹60,000.

The firm was dissolved on 31st March, 2019, on which date, the assets, apart from Cash of ₹70,000, realised ₹14,00,000 and the liabilities were discharged as follows :

(a) Creditors due on 31st May, 2019, were paid off at a discount of 3% per annum.

(b) Bills Payable were discharged at a rebate of ₹1,000.

(c) Workmen Compensation Claim of ₹40,000 was met.

(d) Expenses of dissolution amounting to ₹30,000 were paid.

You are required to prepare :

(i) Realisation Account.

(ii) Partners' Capital Accounts. (I.S.C. 2020)

SOLUTION :

Dr. **REALISATION ACCOUNT** Cr.

Particulars		₹	Particulars		₹
To Sundry Assets[1]		16,30,000	By Sundry Liabilities :		
To Cash A/c :			Creditors	2,00,000	
Creditors	1,99,000		Bills Payables	60,000	
Bills Payables	59,000		Workmen Compensation Reserve	40,000	
Workmen Compensation Claim	40,000		Other Liabilities	3,40,000	6,40,000
Other Liabilities	3,40,000	6,38,000	By Cash A/c (Assets Realised)		14,00,000
To Cash A/c (Exp.)		30,000	By Loss transferred to :		
			Mike's Capital A/c	1,54,800	
			Ajay's Capital A/c	1,03,200	2,58,000
		22,98,000			22,98,000

Dr. **PARTNER'S CAPITAL ACCOUNTS** Cr.

Particulars	Mike	Ajay	Particulars	Mike	Ajay
To Realisation (Loss)	1,54,800	1,03,200	By Bal b/d	6,00,000	4,00,000
To Cash A/c	4,81,200	3,20,800	By Workmen Compensation Reserve	36,000	24,000
	6,36,000	4,24,000		6,36,000	4,24,000

Working Note :

(1) **MEMORANDUM BALANCE SHEET**
as at 31st March, 2019

Liabilities		₹	Assets	₹
Capitals :			Cash	70,000
Mike	6,00,000		Sundry Assets (Balancing figure)	16,30,000
Ajay	4,00,000	10,00,000		
Workmen Compensation Reserve		1,00,000		
Creditors		2,00,000		
Bills Payables		60,000		
Other Liabilities		3,40,000		
		17,00,000		17,00,000

(2) Discount on Creditors : $2,00,000 \times \frac{3}{100} \times \frac{2}{12} = ₹1,000$

MULTIPLE CHOICE QUESTIONS

Select the Best Alternate and tally your answer with the Answers given at the end of the book :

1. In which condition a partnership firm is deemed to be dissolved?
   (A) On a partner's admission
   (B) On retirement of a partner
   (C) On expiry of the period of partnership
   (D) On loss in partnership

2. Court can make an order to dissolve the firm when :
   (A) Some partner has become fully mad
   (B) Partnership deed is fully followed
   (C) Continued future profits are expected
   (D) Firm is running legal business

3. On dissolution of a firm, realisation account is debited with
   (A) All assets to be realised
   (B) All outside liabilities of the firm
   (C) Cash received on sale of assets
   (D) Any asset taken over by one of the partners

4. On dissolution of a firm, out of the proceeds received from the sale of assets .... will be paid first of all.
   (A) Partner's Capital (B) Partner's Loan to Firm
   (C) Partner's additional capital (D) Outside Creditors

5. At the time of dissolution of firm, "Loan of partners" (Loans given by partners to the firm) is paid out of the amount realised on sale of assets :
   (A) After making the payment of loans given by third party
   (B) After making the payment of balance of Capital Accounts of partners
   (C) After making the payment of above (A) and (B)
   (D) Before the payment of loans given by third party

6. At the time of dissolution of firm, at which stage the balance of partner's capital accounts is paid?
   (A) After making the payment to third party's loans
   (B) Before making the payment of partners in respect of their loans
   (C) After making the payment to third party for their loans as well as partners loans
   (D) None of the above.

7. On firm's dissolution, which one of the following account should be prepared at the last?
   (A) Realisation Account (B) Partner's Capital Accounts
   (C) Cash Account (D) Partner's Loan Account

8. In the event of dissolution of a partnership firm, the provision for doubtful debts is transferred to :

(A) Realisation Account
(B) Partners Capital Accounts
(C) Sundry Debtors Account
(D) None of the above

9. On dissolution, if a partner undertakes to make payment of a liability of the firm .... is debited.
(A) Profit & Loss Account
(B) Realisation Account
(C) Partner's Capital Account
(D) Cash Account

10. Unrecorded liability, when paid on dissolution of a firm is debited to :
(A) Partner's Capital A/cs
(B) Realisation A/c
(C) Liabilities A/c
(D) Asset A/c

11. On dissolution of a partnership firm, profit or loss on realisation is distributed among the partners :
(A) In capital ratio
(B) In Profit sharing ratio
(C) Equally
(D) None of the above

12. On dissolution of the firm, amount received from sale of unrecorded asset is credited to :
(A) Partner's Capital Accounts
(B) Profit and Loss Account
(C) Realisation Account
(D) Cash Account

13. Realisation A/c is a :
(A) Nominal A/c
(B) Real A/c
(C) Personal A/c
(D) Real A/c as well as Personal A/c

14. In the event of dissolution of firm, the partner's personal assets are first used for payment of the :
(A) Firm's liabilities
(B) The personal liabilites
(C) None of the two
(D) Any of the two

15. A partnership firm is compulsorily dissolved :
(A) When the business of the firm is declared illegal
(B) When a partner of the firm dies
(C) When a partner of the firm becomes insolvent
(D) When a partner transfers his share to some other person without the consent of other partners

16. At the time of firm's dissolution, Balance of General Reserve shown in the Balance Sheet is credited to :
(A) Realisation Account
(B) Creditor's Account
(C) Partner's Capital Account
(D) Profit & Loss Account

17. On dissolution, goodwill account is transferred to :
(A) In the Capital Accounts of Partners
(B) On the credit of Cash Account
(C) On the Debit of Realisation Account
(D) On the Credit of Realisation Account

18. At the time of dissolution of partnership firm, fictitious assets are transferred to :

(A) Capital Accounts of Partners (B) Realisation Account
(C) Cash Account (D) Partners' Loan Account

19. At time of dissolution of partnership firm, the balance of profit and loss account shown in the assets side of Balance sheet of the firm is transferred to:
(A) Realisation Account (B) Cash Account
(C) Capital Accounts of partners (D) Loan Accounts of partners

20. At the time of dissolution of partnership firm, the amount of 'Bills Payable' shown in the liability side of Balance Sheet is transferred to :
(A) Capital Accounts of Partners (B) Realisation Account
(C) Cash Account (D) Loan Account of Partners

21. On dissolution, the final balance of capital accounts are transferred to :
(A) Realisation Account (B) Cash Account
(C) Profit & Loss Account (D) Loan Accounts of Partners

22. Change in the existing agreement between the partners is called :
(A) Dissolution of Firm (B) Dissolution of Partnership
(C) Dissolution of Business (D) All of the Above

23. On dissolution, the balance of 'Profit & Loss Account' appearing on the assets side of a Balance Sheet is transferred to :
(A) On the debit of Realisation Account
(B) On the credit of Realisation Account
(C) On the debit of Partner's Capital Accounts
(D) On the credit of Partner's Capital Accounts

24. On dissolution of a firm, a partner paid ₹700 for firm's realisation expenses. Which account will be debited?
(A) Cash Account (B) Realisation Account
(C) Capital Account of the Partner (D) Profit & Loss A/c

25. On taking responsibility of payment of realisation expenses by a partner, the account credited will be :
(A) Realisation Account (B) Cash Account
(C) Capital Account of the Partner (D) None of the Above

26. On dissolution of firm, loss calculated in realisation account is debited/credited to which account?
(A) Cash Account (Credit)
(B) Partners' Capital Accounts (Debit)
(C) Partners' Capital Accounts (Credit)
(D) Realisation Account (Debit)

27. Profit or loss of realisation account is transferred to :
(A) Profit & Loss Account (B) Capital Accounts of Partners
(C) Balance Sheet (D) None of the Above

28. Which of the following is transferred to Realisation Account :
(A) Balance of Cash Account (B) Balance of Profit & Loss Account
(C) Amount realised on sale of assets (D) Reserves

29. Which of the following is not transferred to Realisation Account :
(A) Balance of Cash Account
(B) Balance of Reserves
(C) Balance of Profit & Loss Account
(D) All of the Above

30. On taking responsibility of payment of a liability of ₹50,000 by a partner, the account credited will be :
(A) Realisation Account
(B) Cash Account
(C) Capital Account of the Partner
(D) Liability Account

31. Cash balance shown in the Balance Sheet is shown on dissolution of firm in :
(A) Realisation Account
(B) Cash Account
(C) Capital Account
(D) None of the Account

32. On firm's dissolution, on realisation of goodwill (which was shown in Balance Sheet) will be credited to :
(A) Cash A/c
(B) Realisation A/c
(C) Profit & Loss A/c
(D) None of the A/c

HOTS

33. On dissolution of a firm, its Balance Sheet revealed total creditors ₹50,000; Total Capital ₹48,000; Cash Balance ₹3,000. Its assets were realised at 12% less. Loss on realisation will be :
(A) ₹ 6,000
(B) ₹11,760
(C) ₹11,400
(D) ₹ 3,600

34. On firm's dissolution, when a partner voluntarily gives his personal asset to firms' creditor as payment, the account credited will be :
(A) Realisation A/c
(B) Partner's Capital A/c
(C) Cash A/c
(D) None of the A/c

35. On dissolution, when a partner takes over an unrecorded asset, ... is credited.
(A) Capital Account of the Partner
(B) Cash Account
(C) Asset Account
(D) Realisation Account

36. On dissolution, when a partner takes over an asset .... is debited.
(A) Realisation Account
(B) Partner's Capital Account
(C) Cash Account
(D) Asset Account

37. In case of dissolution, assets are transferred to Realisation Account :
(A) At Book Value
(B) At Market Value
(C) Cost or Market Value, whichever is lower
(D) None of the Above

38. On dissolution, the balance of a partner's capital account appearing on the assets side of a balance sheet is transferred to :
(A) On the Debit of Realisation Account
(B) On the Credit of Realisation Account
(C) On the Debit of Partner's Capital Account
(D) On the Credit of Cash Account

39. On dissolution, partner's loan is transferred to :
(A) Partner's Capital Account
(B) Realisation Account
(C) Partner's Loan Account
(D) Revaluation Account

40. Sundry Creditors amounted to ₹8,000. These were paid at a discount of 5%. Realisation account will be debited by ....
(A) ₹8,000
(B) ₹7,600
(C) ₹ 400
(D) ₹8,400

41. There was an Unrecorded asset of ₹2,000 which was taken over by a partner at ₹1,500. Partner's Capital Account will be debited by ....
(A) ₹2,000
(B) ₹1,500
(C) ₹ 500
(D) ₹3,500

42. On dissolution of a firm, an unrecorded furniture of the value of ₹5,000 was taken up by a partner for ₹4,300. Which Account will be credited and by how much amount?
(A) Cash Account by ₹4,300
(B) Realisation Account by ₹700
(C) Partner's Capital Account by ₹5,000
(D) Realisation Account by ₹4,300

43. On the basis of following data, final payment to a partner on firm's dissolution will be made :
Debit balance of Capital Account ₹14,000; Share of his profit on realisation ₹43,000; Firm's asset taken over by him for ₹17,000.
(A) ₹31,000
(B) ₹29,000
(C) ₹12,000
(D) ₹60,000

44. On payment of expenses of dissolution, account will be debited :
(A) Realisation Account
(B) Cash Account
(C) Profit & Loss Account
(D) None of the Above

45. An unrecorded asset was valued at ₹1,00,000. On firm's dissolution, it was sold for 52%. Realisation account will be credited with :
(A) ₹ 52,000
(B) ₹48,000
(C) ₹1,00,000
(D) None of the Above

46. On firm's dissolution, a partner undertook firm's creditors at ₹17,000. In this case the account will be credited :
(A) Creditors A/c
(B) Cash A/c
(C) Realisation A/c
(D) Partner's Capital A/c

47. On dissolution, losses are first of all met :
(A) Out of Capital
(B) Out of Profits
(C) Out of private assets of partners
(D) Out of loan from Bank

48. ....is prepared at the time of dissolution.
(A) Revaluation Account
(B) Profit & Loss Account

(C) Profit and Loss Appropriation Account
(D) Realisation Account

49. While transferring assets to realisation account .... is omitted to be transferred.
(A) Patents (B) Goodwill
(C) Cash (D) Investments

50. If total assets are ₹2,00,000; total liabilities are ₹40,000; amount realised on sale of assets is ₹1,75,000 and realisation expenses are ₹3,000, the profit or loss on realisation will be :
(A) Profit ₹12,000 (B) Loss ₹68,000
(C) Loss ₹28,000 (D) Loss ₹25,000

HOTS

51. On dissolution of a firm, debtors were ₹17,000. Of these ₹500 became bad and the rest realised 60%. Which account will be debited and by how much amount?
(A) Realisation Account by ₹16,500 (B) Profit & Loss Account by ₹500
(C) Cash Account by ₹9,900 (D) Debtors Account by ₹7,100

HOTS

52. In the Balance Sheet Total Debtors appear at ₹50,000 and Provision for Doubtful Debts appear at ₹1,500. How much amount will be realised from Debtors, if bad debts amount to ₹10,000 and remaining debtors are realised at a discount of 5%.
(A) ₹38,000 (B) ₹36,500
(C) ₹36,575 (D) ₹39,500

53. How much amount will be paid to Creditors for ₹25,000 if ₹5,000 of the creditors are not to be paid and the remaining creditors agreed to accept 5% less amount?
(A) ₹18,750 (B) ₹19,000
(C) ₹19,750 (D) ₹20,000

54. *P*, a partner, is to bear all expenses of realisation for which he is to be paid ₹2,000. *P* had to pay realisation expenses of ₹2,500. How much amount will be debited to Realisation Account?
(A) ₹ 500 (B) ₹2,500
(C) ₹4,500 (D) ₹2,000

55. How much amount will be paid to A, if his opening capital is ₹2,00,000 and his share of realisation profit amounts to ₹10,000 and he has taken over assets valuing ₹25,000 from the firm?
(A) ₹2,35,000 (B) ₹1,65,000
(C) ₹2,15,000 (D) ₹1,85,000

HOTS

56. Investments valued ₹2,00,000 were not shown in the books. One of the creditors took over these investments in full satisfaction of his debt of

₹2,20,000. How much amount will be deducted from creditors?

(A) ₹ 20,000 (B) ₹2,20,000
(C) ₹4,20,000 (D) ₹2,00,000

57. If creditors are ₹25,000, capital is ₹1,50,000 and cash balance is ₹10,000, what will be the amount of sundry assets?

(A) ₹1,75,000 (B) ₹1,85,000
(C) ₹1,65,000 (D) ₹1,40,000

58. If opening capitals of partners are *A* ₹3,00,000, *B* ₹2,00,000 and *C* ₹1,00,000 and their drawings during the year are *A* ₹50,000, *B* ₹40,000 and *C* ₹30,000 and creditors are ₹60,000, what will be the amount of assets of the firm?

(A) ₹5,40,000 (B) ₹4,20,000
(C) ₹4,80,000 (D) ₹6,60,000

HOTS

59. If total assets of a firm are ₹12,00,000 and total liabilities are ₹2,40,000, what will be the capitals of *P, Q* and *R* if they share profits in the ratio of their capitals and profit sharing ratio is 1 : 2 : 3 :

(A) *P* ₹4,80,000; *Q* ₹3,20,000; *R* ₹1,60,000
(B) *P* ₹1,60,000; *Q* ₹3,20,000; *R* ₹4,80,000
(C) *P* ₹2,00,000; *Q* ₹4,00,000; *R* ₹6,00,000
(D) *P* ₹6,00,000; *Q* ₹4,00,000; *R* ₹2,00,000

60. On dissolution of a firm, a partner's capital account has a credit balance of ₹42,000. His share of profit in realisation account is ₹9,000. He has paid firm's realisation expenses ₹3,000. He will finally get a payment of :

(A) ₹39,000 (B) ₹42,000
(C) ₹54,000 (D) ₹48,000

61. On dissolution of a firm, a partner took over ₹17,000 investments for ₹14,000. Which one of the following account will be debited/credited with how much amount?

(A) Partner's Capital Account Debit with ₹14,000
(B) Partner's Capital Account Credit with ₹17,000
(C) Realisation Account Credit with ₹17,000
(D) Realisation Account Credit with ₹3,000

62. On dissolution of firm, which item is debited to the realisation account?

(A) Realisation expenses paid by partner
(B) Balance of reserve fund
(C) Amount of unrecorded asset
(D) Creditor's balance shown in the Balance Sheet

HOTS

63. At the time of dissolution of a firm, Creditors are ₹70,000; Partners' capital is ₹1,20,000; Cash Balance is ₹10,000. Other assets realised ₹1,50,000. Profit/Loss in the realisation account will be :

(A) ₹60,000 (Loss) (B) ₹80,000 (Profit)
(C) ₹40,000 (Loss) (D) ₹30,000 (Loss)

HOTS

64. On dissolution of a firm, debtors ₹17,000 were shown in the Balance Sheet. Out of this ₹2,000 became bad. One debtor became insolvent. 70% were recovered from him out of ₹5,000. Full amount was recovered from the balance debtors. On account of this item, loss in realisation account will be :

(A) ₹5,100
(B) ₹1,500
(C) ₹3,500
(D) ₹2,000

HOTS

65. X, Y and Z are partners in a firm in the ratio of 4 : 3 : 2. On firm's dissolution, firm's total assets are ₹70,000, creditors are ₹15,000. Realisation expenses are ₹2,100. Assets realised 15% more than the book-value. Creditors were paid 2% more. For profit/loss on realisation, Y's capital account will be debited/credited with :

(A) Credit ₹8,100
(B) Credit ₹2,700
(C) Debit ₹2,700
(D) Debit ₹2,400

HOTS

66. On dissolution of a firm, firm's Balance Sheet total is ₹77,000. On the assets side of the Balance Sheet items were shown preliminary expenses ₹2,000; Profit & Loss Account (Debit) Balance ₹4,000 and Cash Balance ₹1,800. Loss on realisation was ₹6,300. Total assets (including cash balance) realised will be :

(A) ₹69,200
(B) ₹71,000
(C) ₹64,700
(D) ₹62,900

HOTS

67. On dissolution of a firm, partners' capital accounts balance was ₹63,000; creditors balance was ₹12,000 and profit & loss account debit balance was ₹6,000. Profit on realisation of assets was ₹7,800. Total amount realised from assets was :

(A) ₹81,000
(B) ₹76,800
(C) ₹70,800
(D) ₹None

68. On dissolution of a firm, a partner took-over the investments of ₹15,000 at ₹19,000. By how much amount the Realisation Account will be credited?

(A) ₹4,000
(B) ₹19,000
(C) Nil
(D) ₹23,000

69. Anu, Bina and Charan are partners. The firm had given a loan of ₹20,000 to Bina. On the event of dissolution, the loan will be settled by :

(A) Transferring it to debit side of Realization Account.
(B) Transferring it to credit side of Realization Account.
(C) Transferring it to debit side of Bina's Capital Account.
(D) Bina paying Anu and Charan privately. *(C.B.S.E. Sample Paper, 2015)*

70. Which of the following is not transferred to Realisation Account?

(A) Balance of Profit & Loss A/c
(B) Advertisement Suspense A/c
(C) Partner's Loan
(D) All of the above

71. Which of the following does not result into reconstitution of a firm?
(A) Dissolution of partnership firm.
(B) Dissolution of partnership.
(C) Change in profit-sharing-ratio of existing partners.
(D) Death of a partner. *(C.B.S.E. 2020; Delhi)*

72. Rohan, Mohan and Sohan were partners sharing profits equally. At the time of dissolution of the partnership firm, Rohan's loan to the firm will be :
(A) Credited to Rohan's Capital Account.
(B) Debited to Realisation Account.
(C) Credited to Realisation Account.
(D) Credited to Bank Account. *(C.B.S.E. 2020; Mumbai, Chennai)*

[See Answers at the end of the book]

ISC SEMESTER I EXAMINATION
SPECIMEN QUESTION PAPER
ACCOUNTS

Maximum marks : 80

Time allowed : One and a half hours

(Candidates are allowed additional 15 minutes for only reading the paper)

All questions of ***Section A*** *are Compulsory.*

All questions from either ***Section B*** *or* ***Section C*** *are Compulsory.*

Each correct answer carries 2 marks.

Select the correct option for each of the following questions.

SECTION A
Answer all questions.

Q. 1. Pick the odd one out from the following:

(*a*) Interest allowed on a loan taken by the firm from a partner

(*b*) Rent due to a partner of the firm for using his premises for business purposes

(*c*) Salary due to the manager of the firm

(*d*) Salary due to a partner of the firm

Q. 2. If the operating cycle of a company cannot be identified, it is assumed to be:

(*a*) 18 months (*b*) 12 months

(*c*) 10 months (*d*) 15 months

Q. 3. Which of the following is *not* shown as a Current Liability in the Balance Sheet of a company prepared as per Schedule III of the Companies Act, 2013?

(*a*) Trade Payable (*b*) Short term Borrowings

(*c*) Deferred Tax Liabilities (*d*) Short term Provisions

Q. 4. The Interest on Calls-in-arrears Account is closed by:

(*a*) Crediting it to Statement of Profit & Loss

(*b*) Crediting it to Profit & Loss Appropriation Account

(*c*) Debiting it to Profit & Loss Appropriation Account

(*d*) Debiting it to Statement of Profit & Loss

Q. 5. The formula for valuing goodwill under the Capitalisation of Super Profits method is:

(*a*) Super profit made by the firm multiplied by the normal rate of return

(*b*) Capital Employed by the firm multiplied by the normal rate of return

(*c*) Capitalised profit of the firm divided by the rate of return

(*d*) Super profit made by the firm divided by the normal rate of return

Q. 6. Ronaldo Ltd. forfeited 300 equity shares of ₹10 each, fully called up, on which ₹5 per share (including premium of ₹1 per share) was received. It later reissued these shares at a discount.

The maximum discount per share, which the company could have given on their reissue would be:

(*a*) ₹6 per share (*b*) ₹5 per share
(*c*) ₹4 per share (*d*) ₹3 per share

Q. 7. Veena and Soma are partners in a firm. They admit Sara on 1st April, 2020, for ¼ share in the profits of the firm. Sara acquired her share as 1⁄12 from Veena and the remaining from Soma.

The sacrificing ratio of the old partners will be:

(*a*) 11 : 12 (*b*) 1 : 1
(*c*) 1 : 2 (*d*) 1 : 11

Q. 8. Arif, Ravi and Ben are partners in a firm sharing profits and losses in the ratio of 6:4:1. Arif guaranteed a minimum profit of ₹16,000 to Ben. The trading profit of the firm for the year ending 31st March, 2021, was ₹1,32,000.

Arif's share in the profits of the firm will be:

(*a*) ₹72,000 (*b*) ₹68,000
(*c*) ₹69,600 (*d*) ₹16,000

Q. 9. Simi, Manu, and Beena are partners in a firm sharing profits and losses in the ratio of 2 : 2 : 1. The balances of their fixed capital accounts on 1st April, 2020, were: Simi ₹1,00,000, Manu ₹1,00,000 and Beena ₹80,000

After the accounts for the year ended 31st March, 2021, were prepared, it was discovered that interest on capital @ 10% per annum had been credited to the partners' current accounts even though it was not provided in the partnership deed.

The error in Simi's capital account / current account will be rectified by:

(*a*) Debiting her capital account with ₹1,200
(*b*) Crediting her current account with ₹1,200
(*c*) Debiting her current account with ₹1,200
(*d*) Crediting her capital account with ₹1,200

Q. 10. Runa and Ria were partners in a firm sharing profits and losses in the ratio of 3 : 1. On 1st April, 2020, Uday is admitted as a new partner in the firm for 3/8th share in the profits on various terms, one of them being his contribution of ₹42,000 as capital.

The new profit-sharing ratio amongst all the partners to be 3 : 2 : 3.

The capitals of Runa and Ria, after taking into account all the terms of admission were ₹61,625 and ₹25,375.

It is decided that the Capital Accounts of Runa and Ria be adjusted in the ratio of their respective share in the profits after admission, any surplus to be adjusted through the Current Account while any deficiency through the Cash Account.

The surplus capital adjusted through current account will be:

(*a*) Ria's debit capital balance of ₹2,625

(*b*) Runa's credit capital balance of ₹2,625

(*c*) Ria's debit capital balance of ₹19,625

(*d*) Runa's credit capital balance of ₹19,625

Q. 11. On 1st April, 2020, Pixie, Nixie and Gypsy entered into a partnership with fixed capitals of ₹60,000, ₹50,000 and ₹30,000 respectively.

On 1st October, 2020, Pixie gave a loan of ₹12,000 to the firm.

The partnership deed contained the following clauses:

(*a*) Interest on drawings to be charged @ 4% per annum.

(*b*) Pixie to be entitled to a rent of ₹2,000 per annum for allowing the firm to carry on the business in his premises.

Nixie withdrew ₹1,000 at the end of the month for the first six months.

Net Profit of the firm for the year ending 31st March 2021 (before any interest but after rent on Pixie's premises) was ₹1,21,000.

(*a*) **The Net Profit of the firm will be:**

(*i*) ₹1,21,000 (*ii*) ₹1,20,640

(*iii*) ₹1,18,640 (*iv*) ₹ 96,640

(*b*) **Interest on Drawings charged from Nixie will be:**

(*i*) ₹340 (*ii*) ₹220

(*iii*) ₹170 (*iv*) ₹ 18.33

Q. 12. Dev, Gautam and Kamal were three partners sharing profits and losses in the ratio of 2 : 1 : 2. On 1st April, 2020, their capital account balances stood at ₹90,000, ₹80,000 and ₹20,000 (Dr.) respectively.

On this date they admitted Naveen into the partnership with a capital of ₹50,000.

Naveen is to have ¼ share of the profits with a guaranteed minimum share of distributable profit of ₹40,000.

The new profit-sharing ratio among the partners being Dev : Gautam : Kamal : Naveen = 6 : 2 : 7 : 5.

The profit of the firm for the year 2020-21 was ₹1,60,000 before the following adjustments were made:

- Interest on Capital @ 10% per annum to be allowed to the partners.
- Interest on Drawings: Dev: ₹3,000; Kamal: ₹6,000.
- Salary to Partners: Gautam ₹7,000; Naveen: ₹10,000.

(*a*) **The sacrificing ratio of Dev, Gautam and Kamal will be:**

(*i*) 2 : 1 : 2 (*ii*) 2 : 2 : 1

(*iii*) 2 : –2 : 1 (*iv*) 2 : –1 : 2

(*b*) **The total interest on capital allowed by the firm to the partners will be:**

(*i*) ₹22,000 (*ii*) ₹23,000
(*iii*) ₹21,400 (*iv*) ₹23,100

(*c*) **Deficiency in Naveen's profits will be:**

(*i*) ₹ 8,000 (*ii*) ₹ 7,500
(*iii*) ₹12,500 (*iv*) ₹12,000

Q. 13. Ritesh and Somesh are partners in a firm sharing profits and losses equally.

They admit Satvik on 1st April, 2021 for ⅕ share in the profits of the firm, future profit-sharing ratio between Ritesh and Somesh would be 3:2.

At the time of reconstitution of a partnership firm, goodwill was valued at two years' purchase of the average profits of the preceding four years which were as follows:

Year	*Profit/Loss*		
2017-18	Profit	₹70,000	(after debiting loss of stock by fire ₹15,000)
2018-19	Profit	₹50,000	(including insurance claim of ₹5,000)
2019-20	Loss	₹40,000	(after debiting voluntary retirement compensation paid ₹20,000)
2020-21	Profit	₹60,000	(excluding insurance premium of ₹10,000 on insurance of assets)

(*a*) **The average profits of the firm from the year 2017-18 to the year 2020-21 were:**

(*i*) ₹30,000 (*ii*) ₹60,000
(*iii*) ₹37,500 (*iv*) ₹40,000

(*b*) **The value of goodwill of the firm on Satvik's admission was:**

(*i*) ₹60,000 (*ii*) ₹ 80,000
(*iii*) ₹75,000 (*iv*) ₹1,20,000

(*c*) **Satvik is unable to bring in cash his share of goodwill. The account to be debited to record his goodwill compensation will be:**

(*i*) Satvik's Capital A/c (*ii*) Satvik's Current A/c
(*iii*) Premium for Goodwill A/c (*iv*) Old Partners' Capital A/c

Q. 14. Dhruv and Ansh are partners in a firm sharing profits and losses: Dhruv 75% and Ansh 25%. Their Balance Sheet as at 31st March, 2021 is given below:

Balance Sheet of Dhruv and Ansh
As at 31st March, 2021

Liabilities		₹	*Assets*		₹
Sundry Creditors		49,000	Cash		62,000
Workmen Comp. Reserve		5,000	Sundry Debtors	18,500	
Capital A/c:			*Less:* Prov. for		
Dhruv	30,000		Doubtful Debts	(1,500)	17,000

Ansh	20,000	50,000	Land and Building	25,000
		1,04,000		1,04,000

On 1st April 2021, Kavi is admitted as a new partner on the following terms:

(*i*) Land and building is found to be valued at 25% above cost. It is decided to bring it to its cost.

(*ii*) Bad debts amounting to ₹1,800 are to be written off. The remaining debtors are good.

(*iii*) Creditors include an amount of ₹5,000 received as commission from Amar. The necessary adjustment is required to be made.

(*iv*) The liability on Workmen Compensation Reserve is determined at ₹3,000.

(*v*) Kavi is to pay ₹15,000 to the existing partners as premium for Goodwill for 20% of the future profits of the firm. He is also to bring in ₹25,000 as capital.

(*a*) **At the time of Kavi's admission, the Workmen Compensation Reserve of:**

(*i*) ₹5,000 will be credited to the capital accounts of all the partners

(*ii*) ₹3,000 will be credited to the capital accounts of all the partners.

(*iii*) ₹2,000 will be credited to the capital accounts of the old partners.

(*iv*) ₹2,000 will be debited to the capital accounts of the old partners.

(*b*) **The value of Land & Building in the Balance Sheet of the reconstituted firm will be:**

(*i*) ₹20,000 (*ii*) ₹31,250

(*iii*) ₹ 5,000 (*iv*) ₹ 6,250

(*c*) **To adjust the creditors in adjustment (iii):**

(*i*) Commission A/c will be credited with ₹5,000.

(*ii*) Creditors A/c will be credited with ₹5,000.

(*iii*) Amar's A/c will be debited with ₹5,000.

(*iv*) Creditors A/c will be debited with ₹5,000.

(*d*) **The provision for Doubtful Debts in the reconstituted firm will be:**

(*i*) ₹1,500 (*ii*) ₹1,800

(*iii*) Nil (*iv*) None of the above

(*e*) **The date of the Balance Sheet of the reconstituted firm will be:**

(*i*) Balance Sheet for the year ending 31st March, 2022.

(*ii*) Balance Sheet as at 31st March, 2021.

(*iii*) Balance Sheet for the year ending 1st April, 2021.

(*iv*) Balance Sheet as at 1st April, 2021.

Q. 15. ABC Ltd. forfeited 4,000 shares of ₹10 each, fully called up, on which application money of ₹3 had been paid. Out of these 2,000 shares were re-issued as fully paid up. Upon their reissue, the company transferred ₹4,000 to capital reserve.

The rate at which these shares were reissued were:

(*a*) ₹10 per share (*b*) ₹4 per share
(*c*) ₹ 9 per share (*d*) ₹8 per share

Q. 16. Xylo Ltd. was formed on 1st April, 2018, with an authorized capital of ₹12,00,000 divided into equity shares of ₹10 each.
It invited applications for 30,000 shares to be issued at par, in the year of its formation, all of which were subscribed for and the amount due on them fully received.
On 1st April, 2020, the company issued another 60,000 shares at a premium of ₹2 per share to be received with allotment. It received applications for 55,000 shares which were duly allotted.
All amounts due on the allotted shares was received except the final call of ₹2 per share on 1,000 shares. The company forfeited these shares and later reissued 800 of the forfeited shares @ ₹7 per share fully called up.
The Balance Sheet of the company was prepared as at 31st March, 2021, as per Schedule III of the Companies Act, 2013.

(*a*) **The issued capital of the company to be shown in Notes to Accounts as at 31st March, 2021, under 'Share Capital' will be:**

(*i*) ₹12,00,000 (*ii*) ₹9,00,000
(*iii*) ₹ 8,50,000 (*iv*) ₹8,49,600

(*b*) **The subscribed shares of the company at the end of the year 2020-21 will be:**

(*i*) 1,20,000 (*ii*) 90,000
(*iii*) 85,000 (*iv*) 84,800

(*c*) **The amount of Share Capital to be shown in the Balance Sheet of the company as at 31st March, 2021, will be:**

(*i*) ₹12,00,000 (*ii*) ₹9,00,000
(*iii*) ₹ 8,50,000 (*iv*) ₹8,49,600

(*d*) **The net gain made by the company on reissue of the 800 shares will be transferred to:**

(*i*) Reserve Capital Account
(*ii*) Capital Reserve Account
(*iii*) Securities Premium Reserve Account
(*iv*) Statement of P/L

Q. 17. **Journal of Mekon Ltd.**

Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
				₹	₹
	Share Capital A/c	Dr.		.....(a).....	
	Securities Premium Reserve A/c	Dr.		2,000	
	To Share Forfeiture A/c				—
	To Calls-in-Arrears A/c				7,000
	(Being .... shares forfeited for non-payment of ₹ .... (b)....... including premium of ₹2 per share)				

Bank A/c Dr.		—	
Share Forfeiture A/c Dr.		.....(c).....	
To Share Capital A/c			.....(d).....
To ....(e).......... A/c			1,400
(Being .... shares reissued at ₹9 per share, fully paid @ ₹12 per share)			
Share Forfeiture A/c Dr.		700	
To Capital Reserve A/c			700
(Being net gain on reissued shares transferred to Capital Reserve)			

Share Forfeiture A/c

Particulars	₹	*Particulars*	₹
To Share Capital A/c	700	By Share Capital A/c	4,000
To Securities Premium Reserve A/c	1,400		
To Capital Reserve A/c	700		
To Balance c/d	1,200		
	4,000		4,000

Note: Face value of share is ₹10 each.

(*a*) **The Share Capital A/c was debited with:**

(*i*) ₹10,000 (*ii*) ₹9,000
(*iii*) ₹12,000 (*iv*) ₹7,000

(*b*) **The shares were forfeited for non-payment of:**

(*i*) ₹10 per share (*ii*) ₹9 per share
(*iii*) ₹12 per share (*iv*) ₹7 per share

(*c*) **At the time of reissue of shares, the Share Forfeiture A/c was debited with:**

(*i*) ₹6,300 (*ii*) ₹7,000
(*iii*) ₹2,100 (*iv*) ₹1,400

(*d*) **At the time of reissue of shares, the Share Capital A/c was credited with:**

(*i*) ₹6,300 (*ii*) ₹7,000
(*iii*) ₹2,100 (*iv*) ₹1,400

(*e*) **At the time of reissue of shares, the account credited with ₹1,400 was:**

(*i*) Calls-in-arrears A/c (*ii*) Capital Reserve A/c
(*iii*) Securities Premium Reserve A/c (*iv*) None of the above

SECTION B

Answer all questions.

Q. 18. The net revenue from operations of Gama Ltd. is ₹14,00,000.
Its Gross profit is ₹9,00,000;

Operating expenses are ₹75,000;

Commission received is ₹5,000;

Profit from sale of fixed asset is ₹10,000.

The Operating Profit Ratio of Gama Ltd. will be:

(*a*) 59.29% (*b*) 58.92%

(*c*) 60% (*d*) 58.93%

Q. 19. Which of the following four companies is *not* deriving the benefit of 'trading on equity'?

(*a*) Mars Ltd., which has a Debt-Equity Ratio of 0.49:1

(*b*) Venus Ltd., which has a Debt-Equity Ratio of 1.54:1

(*c*) Saturn Ltd., which has a Debt-Equity Ratio of 1.62:1

(*d*) Pluto Ltd., which has a Debt-Equity Ratio of 2.32:1

Q. 20. The particulars of Alpha Ltd. are given below:

Particulars	₹
Equity Share Capital	2,00,000
5% Preference Share Capital	60,000
General Reserve	1,20,000
Fixed Assets	5,05,000
Current Assets	1,20,000
Current Liabilities	40,000
Loan @ 10% Interest	5,00,000
Tax provided during the year	30,000
Profit for the current year after interest and tax (available for the shareholders)	90,000

(*a*) **The Interest Coverage Ratio of the company will be:**

(*i*) 1.8 times (*ii*) 2.8 times

(*iii*) 3.4 times (*iv*) 2.4 times

(*b*) **The Proprietary Ratio of the company will be:**

(*i*) 0.47:1 (*ii*) 0.75:1

(*iii*) 0.61:1 (*iv*) 0.38:1

Q. 21. From the given particulars of Zee Ltd., the Trade Receivables Turnover Ratio of the company will be:

Particulars	₹
Revenue from Operations	12,00,000
Cash Revenue from Operations	25% of Credit Revenue from Operations
Gross Debtors	1,90,000
Bills Receivable	50,000
Provision for Doubtful Debts	10,000

(*a*) 3.75 times (*b*) 4 times

(*c*) 4.17 times (*d*) 8 times

Q. 22. The correct formula for computing Earning per share is:

(*a*) $\dfrac{\text{Net Profit after Tax}}{\text{No. of Shares}}$

(*b*) $\dfrac{\text{Net Profit after Tax and Preference Dividend}}{\text{No. of Shares}}$

(*c*) $\dfrac{\text{Net Profit after Tax and Preference Dividend}}{\text{No. of Equity Shares}}$

(*d*) $\dfrac{\text{Net Profit after Tax and Preference Dividend}}{\text{No. of Preference Shares}}$

Q. 23. The Current Ratio of a company is 1.8:1 and its Quick Ratio is 1.6 : 1.

From the following transactions, pick out the transaction which involves an increase in both the Current Ratio and Quick Ratio:

(*a*) Goods worth ₹10,000 sold at a loss of ₹2,000.

(*b*) Insurance premium of ₹3,000 paid in advance.

(*c*) Plant and Machinery purchased for ₹9,000.

(*d*) Bills Payable of ₹2,000 honoured on the due date.

SOLUTIONS OF ISC SPECIMEN QUESTION PAPER : 2021 FOR SEMESTER I EXAMINATION

1. **Ans.** (*d*) Salary due to a partner of the firm.

Hint :
(a), (b) and (c) are charge against profits. They will be debited to Profit & Loss Account Whereas (d) is appropriation of profit and as such will be debited to Profit & Loss Appropriation Account.

2. **Ans.** (*b*) 12 months.
3. **Ans.** (*c*) Deferred Tax Liabilities
4. **Ans.** (*a*) Crediting it to Statement of Profit & Loss.
5. **Ans.** (*d*) Super profit made by the firm divided by the normal rate of return.
6. **Ans.** (*c*) ₹4
7. **Ans.** (*c*) 1 : 2

Hint : Veena's Sacrifice : $\frac{1}{12}$

Soma's Sacrifice : $\frac{1}{4} - \frac{1}{12} = \frac{3-1}{12} = \frac{2}{12}$

Hence, Sacrifice Ratio $= \frac{1}{12} : \frac{2}{12}$ or 1 : 2

8. **Ans.** (*b*) ₹68,000.

Hint : 1,32,000 Divided in 6 : 4 : 1

Arif's Share $=$ 1,32,000 $\times \frac{6}{11} =$ ₹72,000

Ravi's Share $=$ 1,32,000 $\times \frac{4}{11} =$ ₹48,000

Ben's Share $=$ 1,32,000 $\times \frac{1}{11} =$ ₹12,000

Since, Ben is guaranteed a minimum profit of ₹16,000
Arif's Share = ₹72,000 – ₹4,000 = ₹68,000.

9. **Ans.** (*b*) Crediting Simi's Current Account with ₹1,200

Hint : TABLE SHOWING ADJUSTMENT

Particulars		*Simi*	*Manu*	*Beena*	*Total*
		₹	₹	₹	₹
Cancellation of Interest @10% p.a.	(Dr.)	10,000	10,000	8,000	28,000
Division of ₹28,000 in 2 : 2 : 1	(Cr.)	11,200	11,200	5,600	28,000
		(Cr.) 1,200	(Cr.) 1,200	(Dr.) 2,400	—

10. **Ans.** (d) Runa's Credit Capital balance of ₹19,625.

Hint : Total Capital of the firm based on Uday's Capital : 42,000 $\times \frac{8}{3} =$ ₹1,12,000

		Runa	Ria
		₹	₹
Capitals in the new firm should be :	$1,12,000 \times \frac{3}{8}$	42,000	
	$1,12,000 \times \frac{2}{8}$		28,000
Existing Capitals		61,625	25,375
		Surplus Capital 19,625	Deficiency 2,625

As per agreement, Surplus Capital is to be adjusted through the Current Account and any deficiency through the Cash Account.

Hence, Surplus Capital adjusted through Current Account will be Runa's Capital ₹19,625.

11. (*a*) **Ans.** (*ii*) ₹1,20,640

Hint :		₹
	Net Profit before any interest	1,21,000
	Less : Interest on Loan : $12,000 \times \frac{6}{100} \times \frac{6}{12}$	360
	Net Profit	1,20,640

(*b*) **Ans.** (*iii*) ₹170

Hint : Interest on Drawings for first six months :
Since ₹1,000 per month have been withdrawn at the end of each month, interest for first six months will be $\frac{5+0}{2} = 2.5$ months

	$= 6,000 \times \frac{4}{100} \times \frac{2.5}{12}$	50
Interest on Drawings for last six months	$= 6,000 \times \frac{4}{100} \times \frac{6}{12}$	120
Total Interest on Drawings		170

12. (*a*) **Ans.** (*ii*) 2 : 2 : 1

Hint : Sacrifice by Dev $= \frac{2}{5} - \frac{6}{20} = \frac{8-6}{20} = \frac{2}{20}$

Sacrifice by Gautam $= \frac{1}{5} - \frac{2}{20} = \frac{4-2}{20} = \frac{2}{20}$

Sacrifice by Kamal $= \frac{2}{5} - \frac{7}{20} = \frac{8-7}{20} = \frac{1}{20}$

Hence, Sacrifice Ratio $= \frac{2}{20} : \frac{2}{20} \frac{1}{20} = 2 : 2 : 1$

(*b*) **Ans.** (*i*) ₹22,000

Hint :	Interest on Capitals :	₹
	Dev : 10% on ₹90,000	9,000
	Gautam : 10% on ₹80,000	8,000
	Naveen : 10% on ₹50,000	5,000
		22,000

(c) **Ans.** (*ii*) ₹7,500

			₹
Hint :	Net Profit		1,60,000
	Less : Interest on Capitals	22,000	
	Salary to Partners (₹7,000 + ₹10,000)	17,000	39,000
			1,21,000
	Add : Interest on Drawings (₹3,000 + ₹6,000)		9,000
	Divisible Profit		1,30,000
	Naveen's Share : $1,30,000 \times \frac{1}{4}$		32,500
	Minimum Guaranteed Amount		40,000
	Deficiency		7,500

13. (*a*) **Ans.** (*iv*) ₹40,000

				₹
Hint :	Profit for	2017-18 : ₹70,000 + ₹15,000	=	85,000
		2018-19 : ₹50,000 – ₹5,000	=	45,000
		2019-20 : (₹40,000) + ₹20,000	=	(20,000)
		2020-21 : ₹60,000 – ₹10,000	=	50,000
				1,60,000

Average Profits = $\frac{1,60,000}{4}$ = ₹40,000

(*b*) **Ans.** (*ii*) ₹80,000

(*c*) **Ans.** (*ii*) Satvik's Current Account

14. (*a*) **Ans.** (*iii*) ₹2,000 will be credited to the Capital Accounts of old partners.

(*b*) **Ans.** (*i*) ₹20,000

Hint : Actual Value of Land & Building : $25,000 \times \frac{100}{125}$ = ₹20,000

(*c*) **Ans.** (*iv*) Creditors A/c will be debited with ₹5,000.

(*d*) **Ans.** (*iii*) Nil

(*e*) **Ans.** (*iv*) Balance Sheet as at 1st April, 2021.

15. **Ans.** (*c*) ₹9 per share.

Hint :	Forfeited amount on 2,000 reissued shares = 2,000 × ₹3	6,000
	Transferred to Capital Reserve	4,000
	Loss on Re-issue	2,000

Loss on Reissue per share = $\frac{2,000}{2,000}$ = ₹1 per share.

Hence, shares were reissued for ₹9 per share.

16. (*a*) **Ans.** (*ii*) ₹9,00,000

(*b*) **Ans.** (*iv*) 84,800

(*c*) **Ans.** (iv) 8,49,600

		₹
Hint :	Subscribed and Fully Paid Capital 84,800 Shares of ₹10 each fully paid	8,48,000
	Add : Share Forfeiture Account (₹8 per share received on 200 unissued shares)	1,600
		8,49,600

16. (*d*) **Ans.** (*ii*) Capital Reserve Account

17. **Hint :**

Date	Particulars	L.F.	Dr. Amount ₹	Cr. Amount ₹
	Share Capital A/c Dr.		9,000	
	Securities Premium Reserve A/c Dr.		2,000	
	To Share Forfeiture A/c			4,000
	To Calls in Arrears A/c			7,000
	(1,000 shares forfeited for non-payment of ₹7 per share including premium of ₹2)			
	Note : (*i*) In this entry missing figure of ₹4,000 has been taken from share forfeiture account given in the question.			
	(*ii*) In this entry ₹9,000 is the balancing figure of the entry.			
	Bank A/c Dr.		6,300	
	Share Forfeiture A/c Dr.		2,100	
	To Share Capital A/c			7,000
	To Securities Premium Reserve A/c			1,400
	(700 shares reissued at ₹9 per share, fully paid @ ₹2 per share premium)			
	Note : (*i*) In this entry premium of ₹1,400 is already given and since the shares are reissued @₹2 per share premium, shares reissued are 1,400 ÷ 2 = 700			
	(*ii*) Shares are reissued at ₹9 per share fully paid and ₹2 are to be credited to Securities Premium A/c. As such shares are reissued at a loss of ₹3 per share.			
	(*iii*) Figure of ₹2,100 can also be taken from Share Forfeiture A/c given in the question.			

17. (*a*) **Ans.** (*ii*) ₹9,000
(*b*) **Ans.** (*iv*) ₹7 per share
(*c*) **Ans.** (*iii*) ₹2,100
(*d*) **Ans.** (*ii*) ₹7,000
(*e*) **Ans.** (*iii*) Securities Premium Reserve A/c

SECTION B

18. **Ans.** (a) 59.29%

Hint : Operating Profit Ratio $= \dfrac{\text{Operating Profit}}{\text{Revenue from Operations}} \times 100$

Operating Profit = Gross Profit – Operating Exp. + Operating Income (Commission Received)

$= ₹9,00,000 - ₹75,000 + ₹5,000 = ₹8,30,000$

Operating Profit Ratio $= \frac{8,30,000}{14,00,000} \times 100 = 59.29\%$

19. **Ans.** (*a*) Mars Ltd., which has a Debt-Equity Ratio of 0.49 : 1 is not deriving the benefit of trading on equity.

Note : The use of higher debts in comparison to equity in the Company's Capital structure is called trading on equity. In case the debt funds yield a return greater than the cost of debts, the profits available to equity shareholders will increase. It is termed trading on equity

20. (*a*) **Ans.** (*iii*) 3.4 times

Hint : Interest Coverage Ratio $= \frac{\text{Net Profit before Interest and Tax}}{\text{Fixed Interest Charges}}$

Calculation of Net Profit before Interest and Tax	₹
Net Profit after Interest and Tax	90,000
Add : Tax provided during the year	30,000
Add : Interest on Loan @ 10%	50,000
	1,70,000

Interest Coverage Ratio $= \frac{₹1,70,000}{₹50,000} = 3.4$ times

(*b*) **Ans.** (*ii*) 0.75 : 1

Hint : Proprietary Ratio $= \frac{\text{Shareholder's Funds}}{\text{Total Assets}}$

Shareholder's Funds =	₹
Equity Share Capital	2,00,000
5% Pref. Share Capital	60,000
General Reserve	1,20,000
Surplus i.e. net profit after Interest and Tax	90,000
	4,70,000

Total Assets = Fixed Assets + Current Assets

$= ₹5,05,000 + ₹1,20,000 = ₹6,25,000$

Proprietary Ratio $= \frac{₹4,70,000}{₹6,25,000} = 0.75 : 1$

21. **Ans.** (*b*) 4 times

Hint : Total Revenue from Operations = ₹12,00,000

Ratio of Cash Revenue and Credit Revenue from Operations

= 25 : 100 or 1 : 4

Hence, Credit Revenue from Operations $= ₹12,00,000 \times \frac{4}{5} = ₹9,60,000$

Trade Receivables = Gross Debtors + Bills Receivables

$= ₹1,90,000 + ₹50,000 = 2,40,000$

Trade Receivables Turnover Ratio $= \frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$

$= \frac{₹9,60,000}{₹2,40,000} = 4$ times

22. **Ans.** (*c*)

$\frac{\text{Net Profit after Tax and Preference Dividend}}{\text{No. of Equity Shares}}$

23. **Ans.** (*d*) Bills Payable of ₹2,000 honoured on the due date.

ANSWERS OF MULTIPLE CHOICE QUESTIONS

Chapter 1

Accounting for Partnership Firms — Fundamentals

(A) Answers of Case Based MCQs :

1. (a) **Ans.** (*ii*)
Since interest on Capital is stated as a charge in this question, it will be allowed even though firm has incurred loss.

(b) **Ans.** (*iv*)
Interest on Loan will be allowed @ 6% p.a., it being a charge against profits.

(c) **Ans.** (*iii*)
Interest on Loan to Vandna will not be charged.
In the absence of Partnership Deed, Partnership Act 1932 applies, which does not provide for charging interest on loan to partners.

(d) **Ans.** (*ii*) ₹40,000

Hint :

	₹
Loss for the year	35,000
Add : Interest on Capital :	
Shruti : 8% on 3,00,000	24,000
Vandna : 8% on 2,00,000	16,000
Add : Interest on Loan :	
$2,00,000 \times \frac{6}{100} \times \frac{5}{12}$	5,000
	80,000

Shruti's share of loss : $80,000 \times \frac{1}{2}$ = ₹40,000

2. (a) **Ans.** (*iii*) Credited to Rent Payable Account

(b) **Ans.** (*ii*) Credited to his Current Account

(c) **Ans.** (*ii*) ₹2,00,000

Hint :

	₹
Profit for the year	3,30,000
Less : Rent : ₹10,000 × 12	1,20,000
	2,10,000
Less : Manager's Commission : $2,10,000 \times \frac{5}{105}$	10,000
Net Profit	2,00,000

(d) **Ans.** (*iv*) ₹60,000

Hint :

	₹
Net Profit	2,00,000
Less : Salary to Lalit : ₹20,000 × 4	80,000
	1,20,000

Kanishk's Share = $\frac{1}{2}$ of ₹1,20,000 = ₹60,000

3. (a) **Ans.** (*iii*) ₹57,200

Hint :

		₹
Sale of Sanitisers		1,20,000
Less :	Cost of Goods Sold	(50,000)
	Gross Profit	70,000
Less :	Rent (1,000 × 7)	(7,000)
	Manager's Commission	(5,000)
	Interest on Partner's Loan as per Q. C	(800)
	Net Profit	57,200

(b) **Ans.** (*i*) Profits for the Accounting year.

(c) **Ans.** (*iv*) ₹800

4. (a) **Ans.** (*iii*) Debited to Profit & Loss Account

(b) **Ans.** (*ii*) ₹69,300

Hint :

Dr. PROFIT AND LOSS ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Rent	48,000	By Profit for the year	1,25,000
To Manager's Commission : $77{,}000 \times \frac{10}{100}$	7,700		
To Net Profit tfd. to P & L App. A/c	69,300		
	1,25,000		1,25,000

(c) **Ans.** (*iv*) Mukesh ₹41,580 and Navdeep ₹27,720

Hint :

		₹
Interest on Mukesh's Capital	: 8% on ₹6,00,000	48,000
Interest on Navdeep's Capital	: 8% on ₹4,00,000	32,000
		80,000

Since available profit is only ₹69,300 which is less than interest payable ₹80,000, profit will be distributed in the ratio of interest on Capital i.e., ₹48,000 : ₹32,000 or 3 : 2.

Mukesh's Share $= 69{,}300 \times \frac{3}{5} = ₹41{,}580$

Navdeep's Share $= 69{,}300 \times \frac{2}{5} = ₹27{,}720$

(d) **Ans.** (*ii*) Nil

5. (a) **Ans.** (*iii*) ₹4,050

Hint :

Interest on Trisha's Drawings :

$$72{,}000 \times \frac{9}{100} \times \frac{7.5}{12} = ₹4{,}050$$

(b) **Ans.** (*iii*) On the Credit Side of Current Accounts

(c) **Ans.** (*iv*) ₹40,000

Hint :

PROFIT & LOSS APPROPRIATION ACCOUNT

Dr. Cr.

Particulars		₹	*Particulars*		₹
To Interest on Capital :			By Profit & Loss A/c		1,20,440
Shashi	30,000		By Interest on Drawings :		
Trisha	18,000	48,000	Shashi*	3,510	
To Profit tfd. to :			Trisha	4,050	7,560
Shashi's Current A/c	40,000				
Trisha's Current A/c	40,000	80,000			
		1,28,000			1,28,000

* $72{,}000 \times \frac{9}{100} \times \frac{6.5}{12} = ₹3{,}510$

(d) **Ans.** (*i*) ₹5,510

SHASHI'S CURRENT ACCOUNT

Dr. Cr.

Particulars	₹	*Particulars*	₹
To Drawings	72,000	By Interest on Capital	30,000
To Interest on Drawings	3,510	By Profit & Loss App. A/c	40,000
		By Balance c/d	5,510
	75,510		75,510

(e) **Ans.** (*iv*) On the Credit Side of Profit & Loss Appropriation Account.

6. (a) **Ans.** (*ii*) ₹1,20,640

Hint :

	₹
Net Profit before any interest	1,21,000
Less : Interest on Loan : $12{,}000 \times \frac{6}{100} \times \frac{6}{12}$	360
Net Profit	1,20,640

(b) **Ans.** (*iii*) ₹170

Hint :

Interest on Drawings for first six months :

Since ₹1,000 per month have been withdrawn at the end of each month,

	₹
Interest for first six months will be $\frac{5+0}{2} = 2.5$ months $= 6{,}000 \times \frac{4}{100} \times \frac{2.5}{12}$	50
Interest on Drawings for last six months $= 6{,}000 \times \frac{4}{100} \times \frac{6}{12}$	120
Total Interest on Drawings	170

7. (a) **Ans.** (*iii*) ₹3,000

Hint :

Interest on Capital will not be allowed but interest on Loan will be allowed @ 6% p.a. for six months.

(b) **Ans.** (*iv*) No Interest will be charged

(c) **Ans.** (*iv*) Cannot be admitted since all partners should agree.

(d) **Ans.** (*i*) ₹36,000

Hint :

Date	*Particulars*		*L.F.*	*Dr. Amount*	*Cr. Amount*
				₹	₹
	Ayush's Capital A/c	Dr.		60,000	
	Chaman's Capital A/c	Dr.		40,000	
	Govind's Capital A/c	Dr.		20,000	
	To Profit & Loss A/c				1,20,000
	Ayush's Capital A/c	Dr.		36,000	
	Chaman's Capital A/c	Dr.		54,000	
	To Govind's Capital A/c				90,000

Govind is guaranteed a minimum profit of ₹70,000 whereas share of loss debited to his Capital A/c is ₹20,000. Hence, he will be Credited by ₹90,000 borne by Ayush and Chaman in 2 : 3.

(B) Answers of Multiple Choice Questions :

1. D	2. C	3. A	4. B	5. C
6. B	7. C	8. A	9. D	10. B
11. D	12. B	13. D	14. C	15. D
16. D	17. A	18. D	19. B	20. B
21. D	22. D	23. A	24. D	25. A
26. C	27. B	28. A	29. C	30. D
31. B	32. B	33. B	34. C	35. A
36. C	37. A	38. B	39. D	40. D
41. A	42. B	43. A	44. B	45. D
46. A	47. D	48. A	49. D	50. C
51. D	52. A	53. D	54. A	55. C
56. A	57. C	58. D	59. C	60. D
61. A	62. D	63. B	64. D	65. D
66. C	67. D	68. B	69. B	70. C
71. D	72. A	73. D	74. C	75. C
76. D	77. A	78. D	79. D	80. B
81. A	82. C	83. C	84. B	85. C
86. A	87. B	88. A	89. D	90. C
91. B	92. B	93. C	94. A	95. D

96. C	97. A	98. B	99. B	100. A
101. D	102. B	103. D	104. B	105. C
106. D	107. A	108. B	109. D	110. C
111. C	112. D	113. A	114. D	115. B
116. D	117. B	118. C	119. C	120. D
121. A	122. B	123. B	124. A	125. D
126. C	127. A	128. D	129. B	130. D
131. C	132. D	133. D	134. D	

Chapter 2

Goodwill : Concept and Valuation

(A) Answers of Case Based MCQs

1. (*i*) **Ans.** (B) ₹38,000

Hint :

Goodwill = Super Profit × 3 year's purchase

75,000 = Super Profit × 3

Super Profit $= \frac{75,000}{3} =$ ₹25,000

Capital Employed = Assets = ₹3,80,000

Normal Profit $=$ Capital Employed $\times \frac{\text{Normal Rate of Return}}{100}$

$=$ ₹3,80,000 $\times \frac{10}{100} =$ ₹38,000

(*ii*) **Ans.** (C) ₹25,000

(*iii*) **Ans.** (D) ₹63,000

Hint :

Average Profit = Super Profit + Normal Profit
= ₹25,000 + ₹38,000 = ₹63,000

2. (*i*) **Ans.** (C) ₹2,00,000

Hint :

		Profit (₹)
31st March,	2016 :	1,60,000
	2017 :	(3,00,000)
	2018 : ₹4,60,000 – ₹60,000	4,00,000
	2019 : ₹4,00,000 + ₹40,000	4,40,000
	2020 :	3,00,000
		10,00,000

Average maintainable profit $= \frac{10,00,000}{5} =$ ₹2,00,000

(*ii*) **Ans.** (D) ₹1,80,000

Hint :

12% of ₹15,00,000 = ₹1,80,000

(*iii*) **Ans.** (A) ₹60,000

Hint :

Super Profit = 2,00,000 – 1,80,000 = ₹20,000

Goodwill = 20,000 × 3 = ₹60,000

(B) Answers of Multiple Choice Questions :

1. D	2. D	3. B	4. A	5. D
6. B	7. B	8. B	9. C	10. A
11. C	12. B	13. C	14. B	15. D
16. A				

Chapter 3

Admission of a Partner

(A) Answers of Case Based MCQs :

1. (a) **Ans.** (*ii*) 2 : 2 : 1

Hint :

Sacrifice by Dev $= \frac{2}{5} - \frac{6}{20} = \frac{8-6}{20} = \frac{2}{20}$

Sacrifice by Gautam $= \frac{1}{5} - \frac{2}{20} = \frac{4-2}{20} = \frac{2}{20}$

Sacrifice by Kamal $= \frac{2}{5} - \frac{7}{20} = \frac{8-7}{20} = \frac{1}{20}$

Hence, Sacrifice Ratio $= \frac{2}{20} : \frac{2}{20} : \frac{1}{20} = 2 : 2 : 1$

(b) **Ans.** (*i*) ₹22,000

Hint :

	₹
Interest on Capitals :	
Dev : 10% on ₹90,000	9,000
Gautam : 10% on ₹80,000	8,000
Naveen : 10% on ₹50,000	5,000
	22,000

(c) **Ans.** (*ii*) ₹7,500

Hint :

		₹
Net Profit		1,60,000
Less : Interest on Capitals	22,000	
Salary to Partners (₹7,000 + ₹10,000)	17,000	39,000
		1,21,000
Add : Interest on Drawings (₹3,000 + ₹6,000)		9,000
Divisible Profit		1,30,000
Naveen's Share : $1,30,000 \times \frac{1}{4}$		32,500
Minimum Guaranteed Amount		40,000
Deficiency		7,500

2. (a) **Ans.** (*iv*) ₹40,000

Hint :

	₹
Profit for 2017-18 : ₹70,000 + ₹15,000	= 85,000

2018-19	: ₹50,000 – ₹5,000	= 45,000
2019-20	: (₹40,000) + ₹20,000	= (20,000)
2020-21	: ₹60,000 – ₹10,000	= 50,000
		1,60,000

$$\text{Average Profits} = \frac{1,60,000}{4} = ₹40,000$$

(b) **Ans.** (*ii*) ₹80,000

(c) **Ans.** (*ii*) Satvik's Current Account

3. (a) **Ans.** (*iii*) ₹2,000 will be credited to the Capital Accounts of old partners.

(b) **Ans.** (*i*) ₹20,000

Hint : Actual Value of Land & Building : $25,000 \times \frac{100}{125} = ₹20,000$

(c) **Ans.** (*iv*) Creditors A/c will be debited with ₹5,000.

(d) **Ans.** (*iii*) Nil

(e) **Ans.** (*iv*) Balance Sheet as at 1st April, 2021.

4. (a) **Ans.** (*ii*) ₹1,00,000

Hint :

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Plant (1)	60,000	By Loss on Revaluation tfd. to Capital A/cs	1,00,000
To Provision for Doubtful Debts (2)	10,000		
To Investments (₹50,000 *less* Reserve ₹20,000)	30,000		
	1,00,000		1,00,000

(1) Actual value of Plant : $3,00,000 \times \frac{100}{125} = ₹2,40,000$

Loss on Revaluation of Plant = 3,00,000 – 2,40,000 = ₹60,000

	₹
(2) Debtors	1,26,000
Less : Bad Debts	6,000
	1,20,000
Provision @ 10% on 1,20,000	12,000
Less : Existing Provision : ₹8,000 – Bad Debts ₹6,000	2,000
Amount Debited to Revaluation Account	10,000

(b) **Ans.** (*iii*) 6 : 4 : 2 : 3

Hint :

A's Share $= \frac{2}{5}$: D's share $= \frac{1}{5}$: Remaining Share $= 1 - \frac{2}{5} - \frac{1}{5} = \frac{2}{5}$

This will be divided between B and C in their existing ratio 2 : 1

B's new share $= \frac{2}{5} \times \frac{2}{3} = \frac{4}{15}$

C's new share $= \frac{2}{5} \times \frac{1}{3} = \frac{2}{15}$

New Share of A, B, C and $D = \frac{2}{5} : \frac{4}{15} : \frac{2}{15} : \frac{1}{5} = 6:4:2:3$

(c) **Ans.** (*ii*)

(d) **Ans.** (*i*) ₹3,72,000

(e) **Ans.** (*iv*) ₹3,52,000

Hint :

Dr. CAPITAL ACCOUNTS Cr.

Particulars	*A*	*B*	*Particulars*	*A*	*B*
	₹	₹		₹	₹
To Revaluation (Loss)	40,000	40,000	By Balance b/d	4,00,000	3,00,000
To Advertisement Suspense A/c	24,000	24,000	By Premium for Goodwill		80,000
To Balance c/d	3,72,000	3,52,000	By Contingency Reserve	36,000	36,000
	4,36,000	4,16,000		4,36,000	4,16,000

5. (a) **Ans.** (*iii*) Gain ₹1,80,000

Hint :

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	*Particulars*	₹
To Provision for Workmen Compensation Claim	30,000	By Building*	1,50,000
To Gain on Revaluation tfd. to Capital A/cs	1,80,000	By Unrecorded Asset	60,000
	2,10,000		2,10,000

* Actual Value of Building : $6,00,000 \times \frac{100}{80}$ = ₹7,50,000

Gain on Revaluation of Building : 7,50,000 – 6,00,000 = ₹1,50,000

(b) **Ans.** (iv) 7 : 5 : 3 : 3

Sacrifice by A $= \frac{1}{6} \times \frac{2}{3} = \frac{2}{18}$

Sacrifice by B $= \frac{1}{6} \times \frac{1}{3} = \frac{1}{18}$

A's new share $= \frac{3}{6} - \frac{2}{18} = \frac{9-2}{18} = \frac{7}{18}$

B's new share $= \frac{2}{6} - \frac{1}{18} = \frac{6-1}{18} = \frac{5}{18}$

New Share of A, B, C and $D = \frac{7}{18} : \frac{5}{18} : \frac{1}{6} : \frac{1}{6}$ or 7 : 5 : 3 : 3

(c) **Ans.** (*iii*)

(d) **Ans.** (*iii*)

(e) **Ans.** (*i*)

Hint :

	₹
A's Capital A/c	5,00,000
+ Gain on Revaluation	90,000
+ Share in Goodwill	40,000
	6,30,000

6. (a) **Ans.** (*iv*) ₹54,000

Hint :

REVALUATION A/C

Dr. Cr.

Particulars	₹	Particulars		₹
To Machinery	60,000	By Accrued Income		10,600
To Furniture	25,000	By Bad Debts Recovered		30,000
To Bad Debts (₹10,000 – ₹8,000)	2,000	By Loss tfd. to Capital Accounts :		
To Provision for Doubtful Debts (4% of 1,90,000)	7,600	*A*	27,000	
		B	18,000	
		C	9,000	54,000
	94,600			94,600

(b) **Ans.** (*iii*) 4 : 1 : 1 : 2

Hint :

Sacrifice Ratio of *B* and *C* : 2,50,000 : 50,000 or 5 : 1

D's Share is $\frac{1}{4}$

B's Sacrifice $= \frac{1}{4} \times \frac{5}{6} = \frac{5}{24}$

C's Sacrifice $= \frac{1}{4} \times \frac{1}{6} = \frac{1}{24}$

B's New Share $= \frac{2}{6} - \frac{5}{24} = \frac{8-5}{24} = \frac{3}{24}$

C's New Share $= \frac{1}{6} - \frac{1}{24} = \frac{4-1}{24} = \frac{3}{24}$

New Ratio of *A*, *B*, *C* and *D* $= \frac{3}{6} : \frac{3}{24} : \frac{3}{24} : \frac{1}{4} = 12 : 3 : 3 : 6$ OR 4 : 1 : 2 : 2

(c) **Ans.** (*ii*) ₹3,28,000

(d) **Ans.** (*i*) ₹2,26,000

Hint :

CAPITAL ACCOUNTS
(*B*'s Capital A/c need not be prepared)

Dr. Cr.

Particulars	*A* ₹	*C* ₹	Particulars	*A* ₹	*C* ₹
To Goodwill			By Balance b/d	4,00,000	2,00,000

(Written off)	60,000	20,000	By Gen. Res.	15,000	5,000
To Revaluation (Loss)	27,000	9,000	By Premium for		
To Balance c/d	3,28,000	2,26,000	Goodwill		50,000
	4,15,000	2,55,000		4,15,000	2,55,000

(B) Answers of Multiple Choice Questions :

1.	C	2.	B	3.	D	4.	B	5.	B
6.	D	7.	A	8.	C	9.	B	10.	D
11.	A	12.	C	13.	C	14.	D	15.	C
16.	C	17.	A	18.	B	19.	A	20.	C
21.	A	22.	D	23.	B	24.	D	25.	D
26.	C	27.	D	28.	D	29.	C	30.	D
31.	B	32.	A	33.	B	34.	D	35.	B
36.	D	37.	A	38.	C	39.	B	40.	B
41.	C	42.	D	43.	B	44.	C	45.	C
46.	C	47.	A	48.	A	49.	A	50.	C
51.	B	52.	B	53.	A	54.	B	55.	D
56.	C	57.	C	58.	D	59.	C	60.	A
61.	C	62.	C	63.	B	64.	C	65.	B
66.	D	67.	D	68.	D	69.	C	70.	A
71.	B	72.	D	73.	A	74.	B	75.	B
76.	B	77.	D	78.	A				

Chapter 4

Retirement or Death of a Partner

Answers of Multiple Choice Questions :

1.	A	2.	B	3.	A	4.	B	5.	B
6.	D	7.	A	8.	C	9.	A	10.	B
11.	D	12.	C	13.	C	14.	B	15.	C
16.	B	17.	C	18.	A	19.	B	20.	B
21.	C	22.	C	23.	D	24.	A	25.	B
26.	D	27.	C	28.	C	29.	B	30.	C
31.	D	32.	C	33.	B	34.	D	35.	B
36.	B	37.	C	38.	B	39.	D	40.	D
41.	D	42.	C	43.	D	44.	C	45.	B
46.	A	47.	D	48.	C				

Working Q. 48 :

Aggregate (Total) Profits of two years = ₹57,000 + ₹63,000 = ₹1,20,000

Tanvi's Share for 7 months = ₹1,20,000 $\times \frac{7}{12} \times \frac{2}{10}$ = ₹14,000

Chapter 5

Dissolution of a Partnership Firm

Answers of Multiple Choice Questions :

1. C	2. A	3. A	4. D	5. A
6. C	7. C	8. A	9. B	10. B
11. B	12. C	13. A	14. B	15. A
16. C	17. C	18. A	19. C	20. B
21. B	22. B	23. C	24. B	25. C
26. B	27. B	28. C	29. D	30. C
31. B	32. B	33. C	34. B	35. D
36. B	37. A	38. C	39. C	40. B
41. B	42. D	43. C	44. A	45. A
46. D	47. B	48. D	49. C	50. C
51. C	52. A	53. B	54. D	55. D
56. B	57. C	58. A	59. B	60. C
61. A	62. A	63. D	64. C	65. B
66. C	67. B	68. B	69. C	70. D
71. A	72. D			

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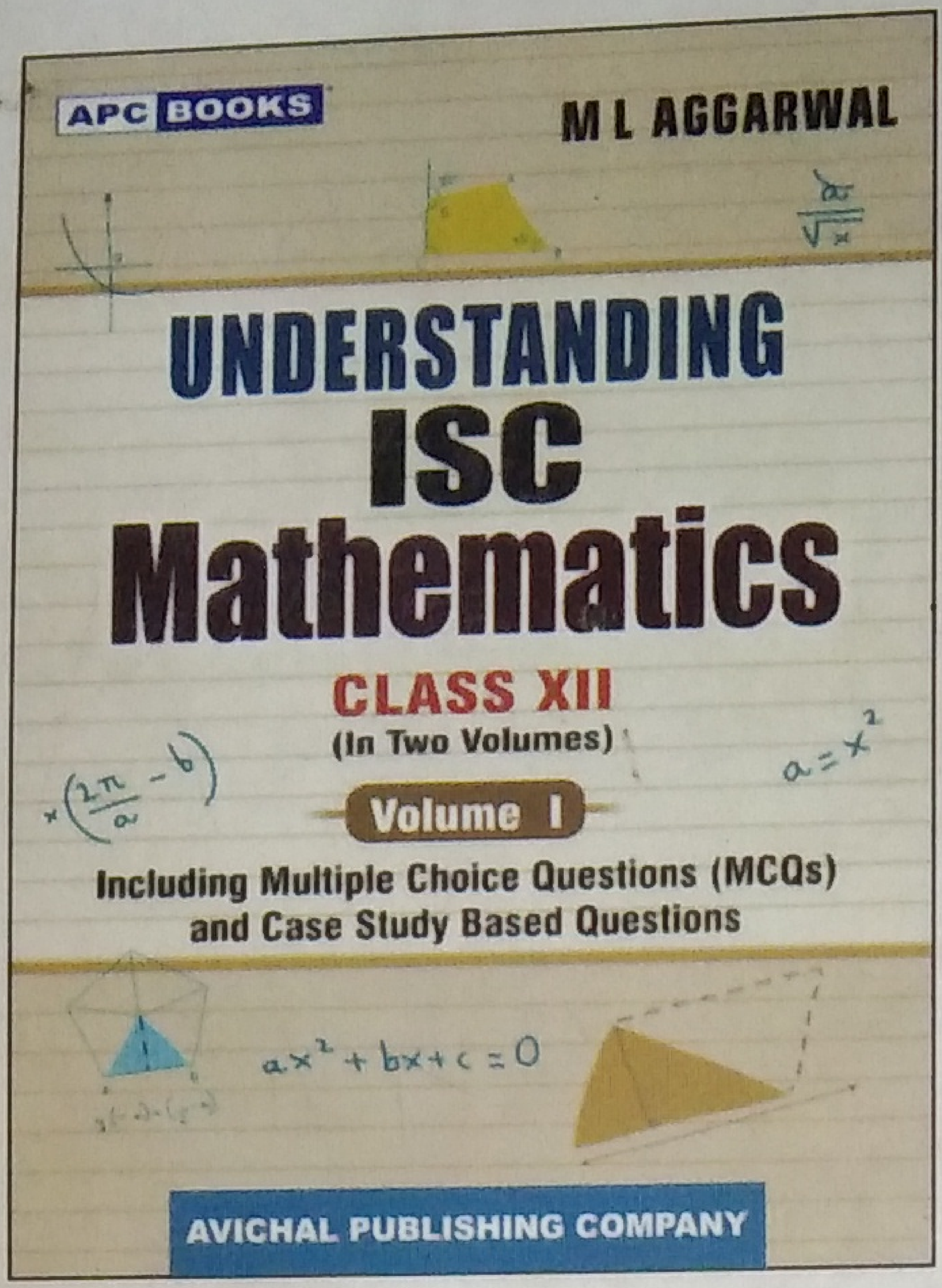

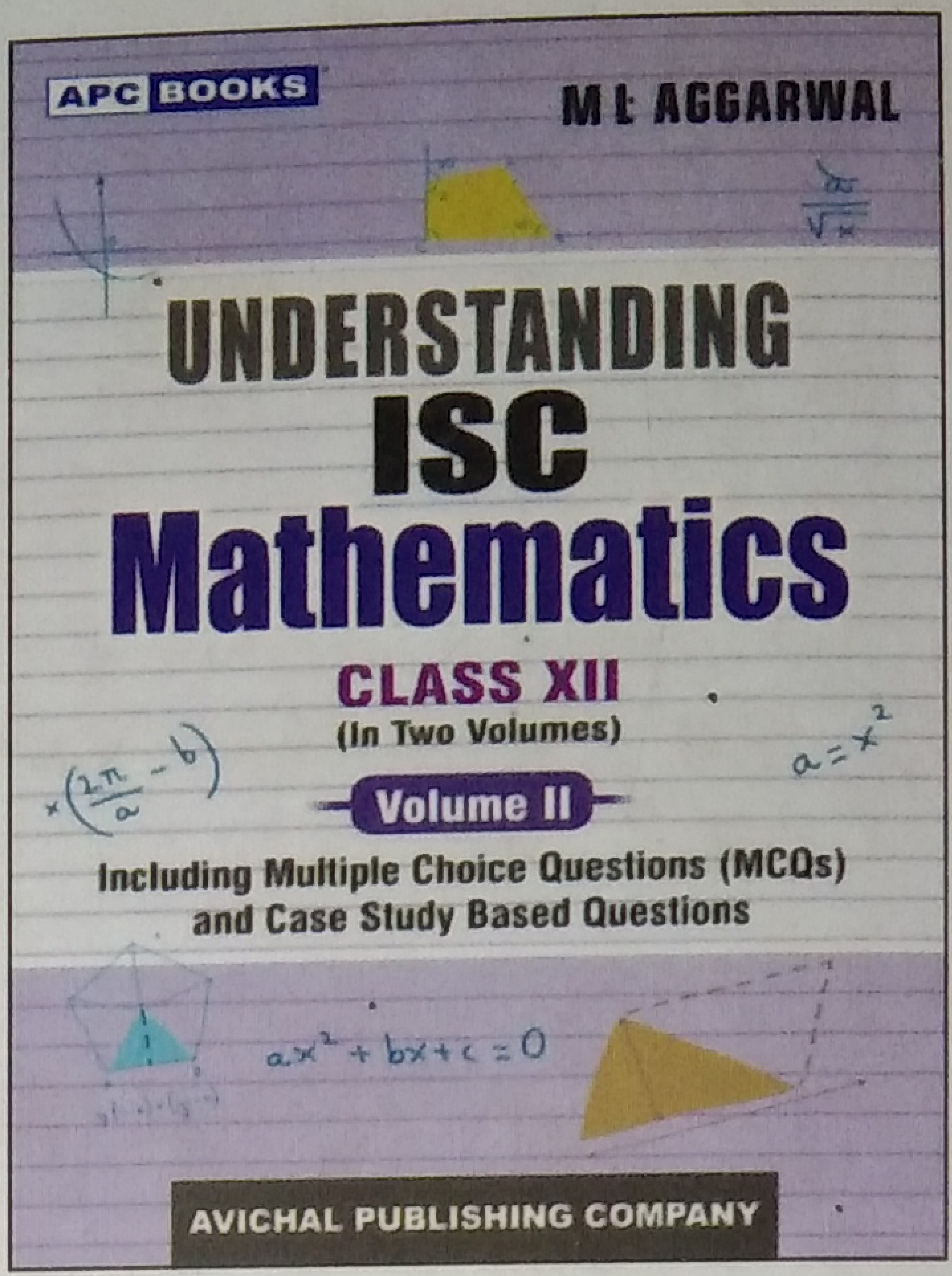

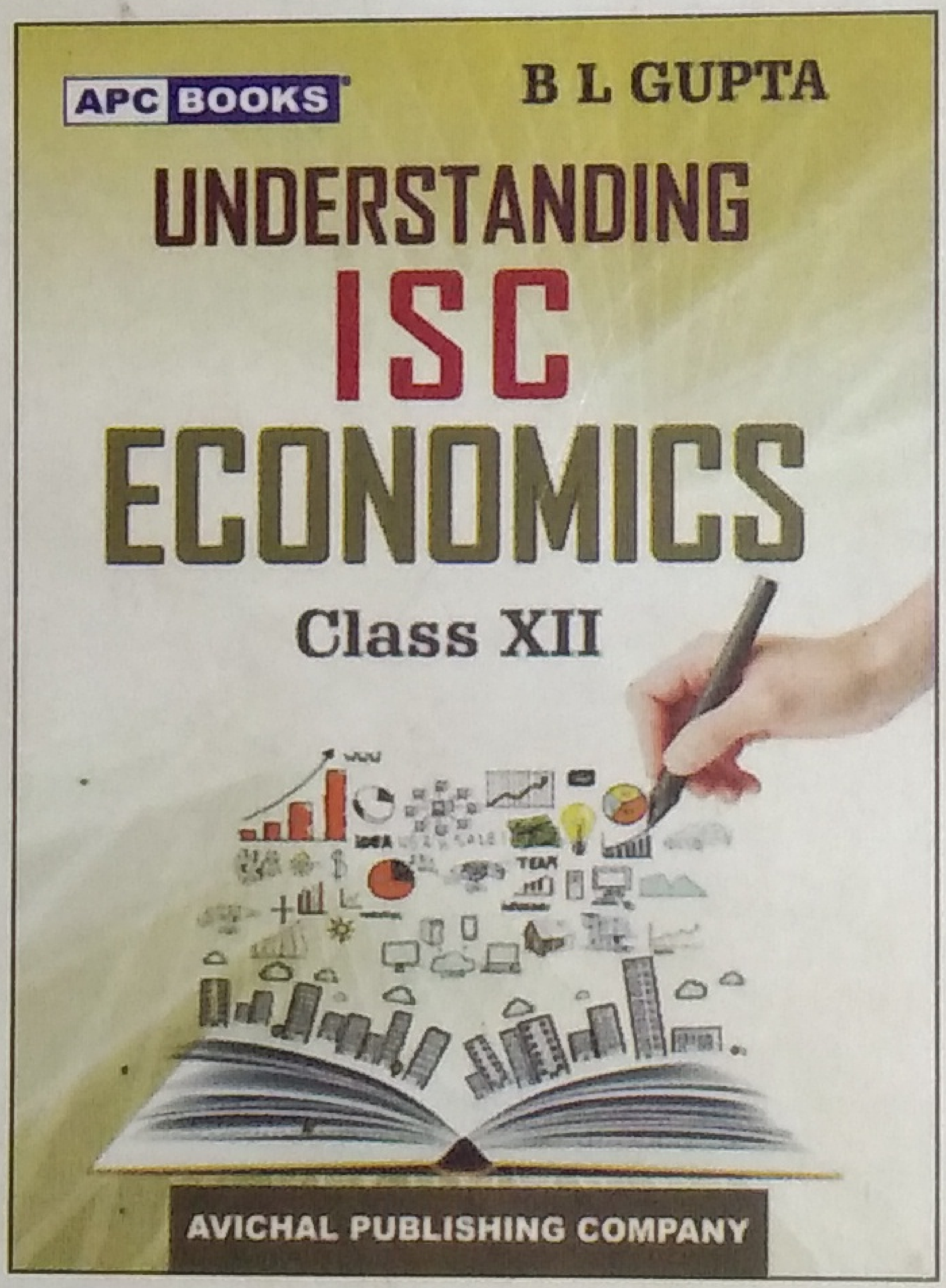

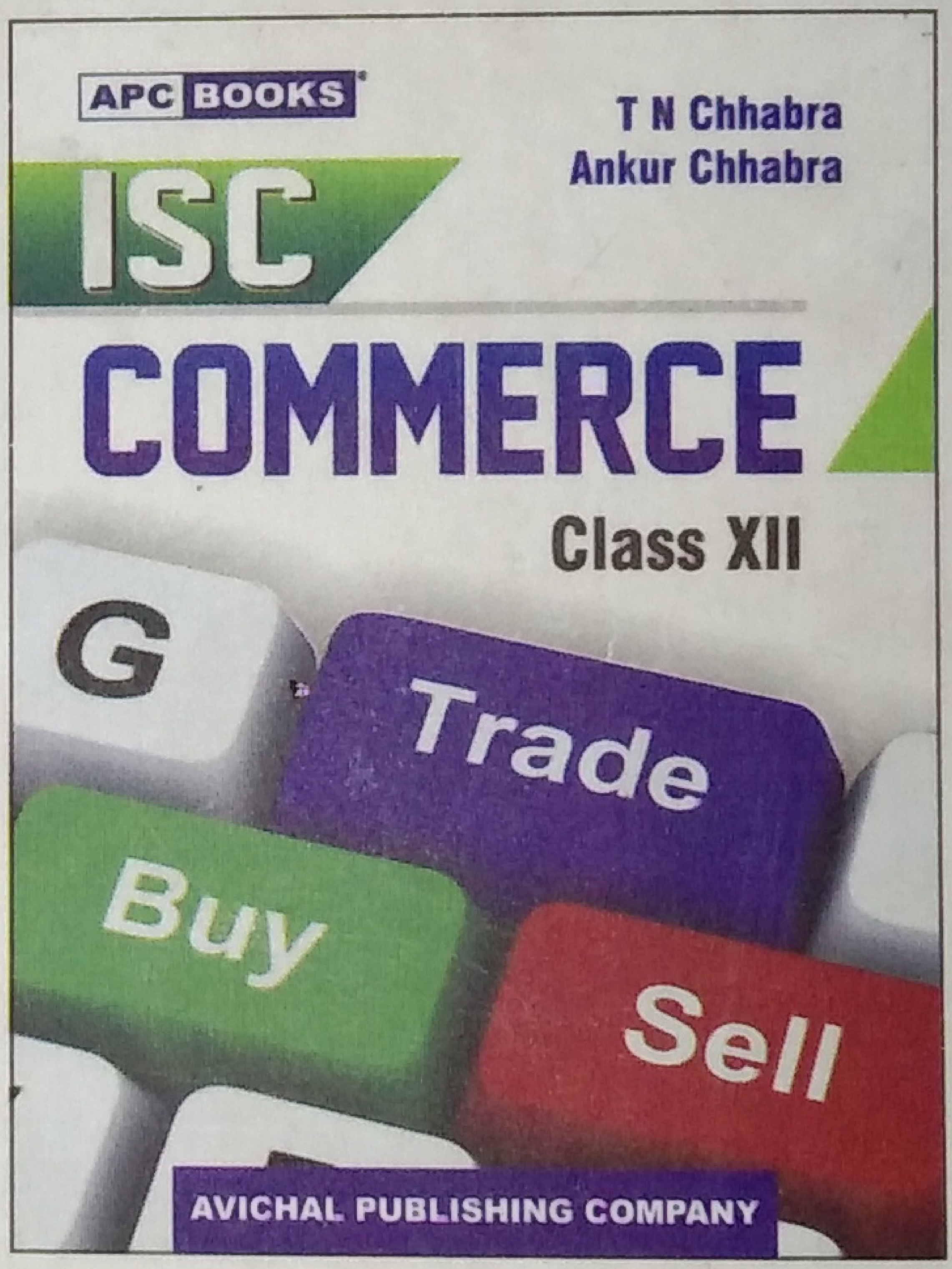

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